Objection Deadline: July 29, 2012

GIBSON, DUNN & CRUTCHER LLP
Michael A. Rosenthal (MR-7006)
Janet M. Weiss (JM-5460)
Craig H. Millet (admitted *pro hac vice*)
Matthew K. Kelsey (MK-3137)
200 Park Avenue
New York, New York 10166-0193
Telephone: (212) 351-4000
Facsimile: (212) 351-4035

Attorneys for the Debtors
and Debtors in Possession

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

IN RE:	:	**Chapter 11**
ARCAPITA BANK B.S.C.(c), *et al.*,	:	**Case No. 12-11076 (SHL)**
Debtors.	:	**Jointly Administered**

DEBTORS' OBJECTION TO TIDE'S MOTION TO LIFT THE AUTOMATIC STAY

Table of Contents

Page

Table of Authorities

Page(s)

Cases

Statutes

Other Authorities

Table of Authorities
(continued**)**

Page(s)

Arcapita Bank B.S.C.(c) ("***Arcapita***") and certain of its subsidiaries and affiliates, as debtors and debtors in possession (collectively, the "***Debtors***") hereby object (the "***Objection***") to the motion of Tide Natural Gas Storage I, LP and Tide Natural Gas Storage II, LP (together, "***Tide***") [Docket No. 279] seeking relief from the automatic stay (the "***Motion***"). In support thereof, the Debtors respectfully represent:

PRELIMINARY STATEMENT

1. Without any credible showing of why immediate action is required, Tide seeks to lift the automatic stay so that it can immediately pursue claims for fraud and breach of contract against both Arcapita and Falcon involving complex facts and extensive discovery that has barely begun. Tide seeks at least $120 million in damages from the Debtors and/or rescission of a $515 million sale transaction, while at the same time sidestepping core issues as to what constitutes property of the estate and whether Tide has any superior rights as to estate property.

2. Although Tide cannot show harm warranting an exception to the automatic stay, the estates of all of the Debtors will be harmed if the Debtors are distracted at this crucial time. Tide's Motion comes at a critical time for the Debtors and their reorganization efforts. The Debtors' management and professionals are laser-focused on developing a restructuring plan and securing the funding necessary to expeditiously exit from chapter 11. This full-court press on restructuring initiatives requires undivided attention and maximum effort from the Debtors' skeletal team of dedicated employees. Any distraction during this delicate phase of the chapter 11 process threatens to derail the Debtors' reorganization efforts—to the detriment of all creditors.

3. The action Tide wants to immediately pursue is complex and will involve extensive discovery (including the review and production of tens of thousands of documents),

preparation for at least forty-five party and non-party depositions, resolution of numerous and intricate issues of fact and law, and the expenditure of perhaps millions of dollars in fees for counsel, experts, and vendors. Managing a litigation matter of this size and responding to Tide's burdensome discovery will require substantial time and attention from the Debtors' management—time and attention that should be dedicated to the restructuring efforts. This burden would be especially onerous for those members of the Debtors' senior management whom Tide noticed for depositions. What's more, the Tide litigation has barely proceeded past the pleading phase, may not resolve all related issues, will prejudice the Debtors' other creditors, and cannot proceed until this Court resolves certain core issues fundamental to the issues in the underlying litigation. In these circumstances, the Court should not lift the stay just so that Tide can jump the gun on the claims resolution process to the detriment of other creditors. The Creditors' Committee and the Joint Provisional Liquidators of Arcapita Investment Holdings Limited agree with the Debtors' Objection to the Motion.

BACKGROUND

4. This case focuses on more than $120 million dollars in damages that Tide claims to have suffered, including disputed claims to $70 million in funds placed in escrow as part of the sale of a natural gas storage business by Debtor Falcon Gas Storage Company, Inc. ("***Falcon***") to Tide.

5. Falcon is an indirect wholly owned subsidiary of Debtor Arcapita LT Holdings Limited, which is wholly owned by Debtor Arcapita Investment Holdings Limited, which is in turn wholly owned by Arcapita. Falcon previously owned the majority of the stock of NorTex Gas Storage Company, LLC (together with its subsidiaries, "***NorTex***"), which operated a natural gas storage business. In early 2010, Tide acquired the stock of NorTex from Falcon and minority holders for approximately $515 million (subject to post-closing

adjustments) pursuant to a Purchase Agreement, dated March 15, 2010, between Tide and Falcon, as amended (the "***NorTex Purchase Agreement***"). Arcapita guaranteed certain of Falcon's obligations under the NorTex Purchase Agreement.

6. Prior to closing the NorTex Purchase Agreement, John Hopper and several other then-minority shareholders of Falcon (the "***Hopper Parties***") filed actions against Falcon, certain of its directors, and NorTex, seeking damages and to enjoin the sale of NorTex to Tide (collectively, the "***Hopper Texas Litigation***") based on the allegation that Falcon's board of directors had breached their fiduciary duties by agreeing to a sales price for the NorTex stock below fair value. Although the sale was not enjoined by the courts, as a result of the pending Hopper Texas Litigation and as a condition to closing, Tide insisted that Falcon agree to (1) indemnify Tide for any liability Tide might suffer as a result of the Hopper Texas Litigation, and (2) place approximately $70 million of the total sales proceeds from the NorTex sale in escrow (the "***Escrow Funds***") to be available to satisfy those indemnification obligations.

7. After the NorTex sale closed, on July 27, 2010, Falcon and the Hopper Parties settled the Hopper Texas Litigation in exchange for an immediate cash payment of $6.5 million and also the agreement that, when the Escrow Funds were released to Falcon, Falcon would pay the Hopper Parties an additional $8.25 million. Since the settlement of the Hopper Texas Litigation fully resolved the indemnification agreement giving rise to the Escrow Funds, the closing of the Hopper Texas Litigation settlement resulted in the occurrence of an "Escrow Breakage Event" under the terms of the NorTex Purchase Agreement and Escrow Agreement between Tide and Falcon and the Escrow Funds should have been released at that time.

8. Despite the satisfaction of all conditions set forth in the NorTex Purchase Agreement and Escrow Agreement between Tide and Falcon, including the occurrence of an

"Escrow Breakage Event," Tide refused to allow the release of the Escrow funds and instead filed an action in the Southern District of New York against Falcon, Arcapita, and Arcapita Inc., alleging breach of contract and "fraud in the inducement," among other things. *Tide Natural Gas Storage I, L.P. v. Falcon Gas Storage Co., Inc.*, Case No. 10-cv-05821-KMW (S.D.N.Y.) (before Judge Kimba Wood) (the "***District Court Action***").

9. The District Court Action is a complicated, multi-million dollar suit that is fact-dependent and turns on byzantine analyses relating to, *inter alia*, "volumetric calculations and measurements" that were performed to estimate "the quantities and values of pad gas" located in the NorTex natural gas storage facilities, "the source of compressor fuel and associated operating expense," and "the source of hydrocarbons produced during NGL extraction facility operations…." *See* Mot. ¶¶ 17, 14. If post-hoc forensics demonstrate that any of the intricate analyses and calculations performed by NorTex relating to the foregoing led to unreliable or inaccurate estimates, the District Court Action also involves an inquiry into whether this was something that Falcon's and/or Arcapita's management knew or should have known about.

10. Contrary to Tide's claims, this case is not nearly ready for trial. Although the District Court Action had been pending for about a year and a half at the time it was stayed by Arcapita's bankruptcy filing on March 19, 2012, the case had barely proceeded past the pleading phase; motions for judgment on the pleadings and partial summary judgment were ruled upon on September 29, 2011 and the Debtors' motion for reconsideration was just denied on May 4, 2012. Tide has not produced a single document in discovery. Indeed, at the time of Arcapita's bankruptcy filing, the parties had not even agreed upon the search terms that Tide was to use to identify potentially responsive documents out of millions of electronic documents

possessed by Tide. Although the Debtors have made an initial production of documents, the bulk of the Debtors' documents also have yet to be processed and produced. No depositions have been taken even though the parties have noticed over 45 party and non-party depositions and have served another six document subpoenas that are likely to lead to depositions. The depositions will take months to complete at significant expense since the witnesses are located in Texas, Georgia, Colorado, New York, London, and Bahrain, among other places. Once fact discovery ends, there will be expert discovery on both liability and damages. It is expected that completing discovery will take more than a year and will cost the Debtors more than a million dollars in fees. Simply put, the District Court Action is far from trial.

11. After the District Court Action was stayed by Arcapita's bankruptcy filing, the Hopper Parties filed a motion to intervene in the District Court Action—seeking a declaration that they have an ownership interest in $8.25 million of the Escrow Funds and an order directing the immediate turnover of those funds. *See* District Court Action Docket Nos. 122 and 123. Tide filed a vigorous opposition to the motion to intervene, arguing that the Hopper Parties "do not have a direct interest in the subject of" the District Court Action. *See* District Court Action Docket No. 125 at 5. Before the District Court ruled on the motion to intervene, Falcon filed its bankruptcy petition on April 30, 2012. Thereafter, the Hopper Parties filed an adversary proceeding in this Court (the "***Hopper Adversary***")[1] seeking a declaration that $8.25 million of the Escrow Funds are not property of the Falcon estate and should be immediately turned over to the Hopper Parties. *See* Hopper Adversary Docket No. 1. Despite the competing claims to title to the Escrow Funds, Tide is not named as a party in the Hopper Adversary.

[1] The Hopper Adversary has been assigned case number 12-01662 (SHL).

12. The claims bar date has been set for August 30, 2012 and the Debtors' exclusive right to file a plan of reorganization will now expire on October 15, 2012.

ARGUMENT

A. There is no "Cause" for Lifting the Automatic Stay

13. The automatic stay imposed by section 362(a) of the Bankruptcy Code is "one of the fundamental debtor protections provided by the bankruptcy laws." *Midatlantic Nat'l Bank v. N.J. Dep't of Envtl. Prot.*, 474 U.S. 494, 503 (1986) (internal quotations omitted). The automatic stay "prevents creditors from reaching the assets of the debtor's estate piecemeal and preserves the debtor's estate so that all creditors and their claims can be assembled in the bankruptcy court for a single organized proceeding." *AP Indus., Inc. v. SN Phelps & Co. (In re AP Indus., Inc.)*, 117 B.R. 789, 798 (Bankr. S.D.N.Y. 1990). "'It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy. The automatic stay also provides creditor protection. Without it, certain creditors would not be able to pursue their own remedies against the debtor's property. Those who acted first would obtain payment of the claims in preference to and to the detriment of other creditors . . . .'" *Id.* at 798-99 (quoting H.R. Rep. No. 595, 95th Cong., 1st Sess. 340 (1977); S. Rep. No. 989, 95th Cong. 2d Sess. 49 (1978), reprinted in 1978 U.S.C.C.A.N. 5987, 5963, 6296-97).

14. Section 362 permits the Court to grant relief from the automatic stay only "for cause." 11 U.S.C. § 362(d)(1). The movant bears the initial burden "to produce evidence that cause exists to grant relief from the automatic stay." *In re DBSI, Inc.*, 407 B.R. 159, 166 (Bankr. D. Del. 2009); *see also Sonnax Indus., Inc. v. Tri Component Prods. Corp. (In re Sonnax Indus., Inc.)*, 907 F.2d 1280, 1285 (2d Cir. 1990). "If the movant fails to make an initial showing

of cause . . . the court should deny relief without requiring any showing from the debtor that it is entitled to continued protection." *In re Sonnax Indus., Inc.*, 907 F.2d at 1285.

15. In the Second Circuit, courts look to twelve factors outlined in *Sonnax* to determine whether cause exists to lift the stay.[2] Only those factors relevant to a particular case need be considered, and factors need not be assigned equal weight. *In re Touloumis*, 170 B.R. 825, 828 (Bankr. S.D.N.Y. 1994). Here, the Court should deny the Motion because Tide has not established that cause exists to lift the stay. In fact, each and every relevant *Sonnax* factor militates against lifting the stay.

1. Allowing the District Court Action to Continue Will Interfere With the Bankruptcy Case (Second *Sonnax* Factor)

16. Although much attention is paid to the Escrow Funds, in addition to Falcon, Tide has sued Arcapita as well seeking total damages exceeding $120 million, and Tide seeks relief from stay to proceed immediately with the case as to both Arcapita and Falcon. However, in an attempt to show cause, Tide's motion focuses only on Falcon—claiming that Falcon does not need the breathing spell afforded by chapter 11. Tide cavalierly dismisses the impact that the case will have on Arcapita and the other Debtors overall at a time when the Debtors' full resources are focused on forming a plan of reorganization for the benefit of all creditors. *See* Mot. ¶¶ 35-37. Because of the intertwined nature of the claims asserted, and

[2] The twelve *Sonnax* factors are: "(1) whether relief would result in a partial or complete resolution of the issues; (2) lack of any connection with or interference with the bankruptcy case; (3) whether the other proceeding involves the debtor as a fiduciary; (4) whether a specialized tribunal with the necessary expertise has been established to hear the cause of action; (5) whether the debtor's insurer has assumed full responsibility for defending it; (6) whether the action primarily involves third parties; (7) whether litigation in another forum would prejudice the interests of other creditors; (8) whether the judgment claim arising from the other action is subject to equitable subordination; (9) whether movant's success in the other proceeding would result in a judicial lien avoidable by the debtor; (10) the interests of judicial economy and the expeditious and economical resolution of litigation; (11) whether the parties

because a substantial portion of the relief Tide seeks is against Arcapita, the District Court Action cannot go forward without Arcapita and proceeding against Arcapita now will prejudice all creditors of the Debtors' estates.

17. The District Court Action involves numerous, fact-intensive questions that require extensive discovery to resolve. These include a determination of the accuracy of reporting relating to, *inter alia*, "volumetric calculations and measurements of" "the quantities and values of pad gas" located in the NorTex natural gas storage facilities, "the source of compressor fuel and associated operating expense," and "the source of hydrocarbons produced during NGL extraction facility operations…." *See* Mot. ¶¶ 17, 14. The District Court Action also involves an inquiry into whether Falcon's and/or Arcapita's management knew or should have known about inaccuracies (if any) in the NorTex estimates related to the foregoing. Litigating these multi-faceted issues will require extensive time and attention from the Debtors' management, not to mention the expenditure of more than a million dollars in fees. Courts have routinely declined to lift the stay in similar circumstances where the litigation would divert the attention of the debtor's management and deplete the resources of the debtor's estate. *See, e.g.*, *Borman v. Raymark Indus., Inc.*, 946 F.2d 1031, 1036 (3d Cir. 1991) ("The automatic stay was designed …to forestall the depletion of the debtor's assets due to legal costs in defending proceedings against it; and, in general, to avoid interference with the orderly liquidation or rehabilitation of the debtor.") (quotations and citations omitted); *Johns-Manville Corp. v. Asbestos Litig. Group (In re Johns-Manville Corp.)*, 40 B.R. 219, 223-25 (S.D.N.Y. 1984) (affirming bankruptcy court finding that lifting the Automatic Stay would divert Debtors' and Debtors' employees' attention away from the chapter 11 case and affirming bankruptcy court's

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are ready for trial in the other proceeding; and (12) impact of the stay on the parties and the balance of harms." *In re Sonnax Indus., Inc.*, 907 F.2d at 1286.

denial of motion for relief from the Automatic Stay); *In re Curtis*, 40 B.R. 795, 806 (Bankr. D. Utah 1984) ("Even slight interference with the administration [of a chapter 11 case] may be enough to preclude relief in the absence of a commensurate benefit."); *In re Penn-Dixie Indus., Inc.*, 6 B.R. 832, 836 (Bankr. S.D.N.Y. 1980) ("Interference by creditors in the administration of the estate, no matter how small, through the continuance of a preliminary skirmish in a suit outside the Bankruptcy Court is prohibited.").

18. In fact, Tide concedes that lifting the stay will interfere with the Debtors' bankruptcy cases and may indeed completely supplant the Falcon bankruptcy case. With respect to Falcon, Tide asserts that lifting the stay will "determine the viability of proceeding with the Falcon bankruptcy case…." Mot. ¶ 4. Thus, Tide acknowledges that in seeking to obtain relief from stay, it seeks to deny Falcon the protections of title 11 by continuing litigation intended to disrupt the entire Falcon bankruptcy case and deny it the very purpose of title 11.

19. The distraction and expense of defending a $120 million litigation will interfere with the Arcapita bankruptcy case as well, at a time when Arcapita is developing its reorganization plans. As to Arcapita, Tide simply assumes the false premise that the stay will be lifted as to Falcon, and from that false premise argues that the "marginal cost of lifting the stay as to Arcapita in addition to Falcon is negligible." Mot. ¶ 36. This specious argument conveniently ignores the fact that Arcapita and its management would need to defend any action against Falcon because Falcon does not have its own employees or operations, and the fact that Tide's claims against Falcon and Arcapita are intricately intertwined. Far from being a reason to lift the stay as to Arcapita, the negative impact on Arcapita's case that would result from allowing the District Court Action to continue as to Falcon is sufficient reason to deny the Motion as to Falcon.

2. The District Court Action is Very Far From Trial (Eleventh *Sonnax* Factor)

20. There is no dispute that the "District Court Action is not yet ready for trial…." Mot. ¶ 44. In fact, the District Court Action has barely proceeded past the motion to dismiss stage. Document discovery is in its infancy, with only a fraction of the relevant documents having been produced. Tide has not produced a single document and the parties have not even agreed upon the search terms Tide is to use to identify relevant electronic documents. There are more than 45 depositions to be taken in locations around the world and none of them has even been scheduled. Extensive expert discovery will be needed, none of which has occurred.

21. Although the December 2011 scheduling order listed a trial date of September 10, 2012, it soon became clear to all of the parties that the trial would not occur on that date and that the scheduling order would need to be amended. Counsel had engaged in several discussions about how the schedule was unrealistic and needed to change. As Tide's counsel stated in a March 2012 email: "[T]hink about the schedule and whether it is logical. The amount of documents at issue is vast." Counsel for Tide already stated that it did not intend to produce expert reports in the time frame required in the schedule, and counsel had talked about the earliest realistic trial date being sometime in 2013. The fact that the parties are not ready for trial weighs in favor of keeping the stay in place. *See In re WorldCom, Inc.*, Case No. 02-13533, 2007 WL 841948, at *8 (Bankr. S.D.N.Y. Mar. 12, 2007).

3. The District Court Action Will Not Completely Resolve All Issues (First *Sonnax* factor)

22. Despite Tide's bald assertion that if it prevails on its claims "the Escrow Funds will belong to Tide," the issue of ownership of the Escrow Funds is not before the court in

the District Court Action.[3] Instead, Tide has simply asserted claims in the District Court Action, which if allowed, may be satisfied from the Escrowed Funds, assuming Tide can prove a lien right or other superior interest to those funds ahead of other creditors—which the Debtors deny. Tide has not yet filed a claim in any of the Arcapita chapter 11 cases.

23. Prepetition, Tide did not assert an independent claim of title to the Escrow Funds and the Escrow Funds are simply a potential source for paying a Tide claim, if allowed. Indeed, the NorTex Purchase Agreement and the Escrow Agreement do not provide that Tide retains title to the Escrowed Funds. To the contrary, the Escrow Agreement provides that "for purposes of any Tax based on income, as among the Purchaser [Tide], the Escrow Agent and the Seller [Falcon], the Seller [Falcon] will be treated as the owner of one hundred percent (100%) of the Escrow Account…." Further, the Escrow funds were intended to satisfy any indemnification obligation Falcon may have had to Tide as a result of the Hopper Texas Litigation, which has now been resolved. Therefore, even if its claims are allowed, Tide will not "automatically" and immediately obtain title to the Escrow Funds, and its allowed claims remain to be treated in a plan of reorganization or other disposition under the bankruptcy code. If Tide's argument were correct, then every claimant with an allowed fraud claim in every bankruptcy case would be entitled to a super-priority recovery simply by asserting that the debtor obtained funds based on misrepresentations.

24. No doubt Tide disputes these contentions; however, the very existence of disputed issues as to whether the Escrow Funds are property of the Debtors' estates and also

[3] The Hopper Parties have filed a motion to intervene in the District Court Action to raise the issue of ownership of the Escrow Funds. *See* District Court Action Docket No. 122 and 123. However, Tide filed an opposition to that motion and the Court did not rule on the motion before the case was stayed. Tide has also claimed that it should not be required to give an instruction to the escrow agent to release the Escrow Funds to Falcon pending resolution of

whether Tide has any sort of lien rights or other priority claims to those Escrow Funds, invokes the core jurisdiction of the bankruptcy court. What constitutes property of the estate and whether any lien rights exist as to property of the estate are both core issues to be resolved by the bankruptcy court. 28 U.S.C. § 157(b)(1), (b)(2).

25. Indeed, the issue of ownership of the Escrow Funds is already before this Court as the Hopper Parties have asserted an ownership interest in the Escrow Funds through the Hopper Adversary. Proceedings such as the Hopper Adversary to determine "exemptions from property of the estate" and "orders to turn over property of the estate" are "core" proceedings within the meaning of 28 U.S.C. § 157(b)(2). *See* 28 U.S.C. § 157(b)(2)(B), (E). The resolution of core issues fundamental to the resolution of Tide's underlying claims and the competing claims of the Hopper Parties should be resolved by this Court before resolution of any remaining damage claims.

26. Lifting the stay would deny the Debtors the "breathing spell" afforded by title 11, would deny the Debtors the right to have core issues decided by the bankruptcy court and would force the Debtors to divert scarce resources and energy to a long and arduous legal action involving claims of fraud and breach of contract that will require extensive discovery, depositions, motions, and a complex trial. This process would take well over a year—maybe several years. Further, the resolution of the bankruptcy cases through a plan or plans of reorganization and the treatment of claims in the plan(s) after the consideration of substantive consolidation may greatly impact the treatment of Tide's contingent claim and, hence, both Tide's and the Debtors' desire to engage in protracted and expensive litigation.

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the District Court Action—but that is not the same thing as claiming that it has an extant ownership interest in the funds.

4. Keeping the Stay in Place Will Promote Judicial Economy (Tenth *Sonnax* Factor)

27. "[T]he automatic stay allows the bankruptcy court to centralize all disputes concerning property of the debtor's estate in the bankruptcy court so that reorganization can proceed efficiently, unimpeded by uncoordinated proceedings in other arenas. The Bankruptcy Code provides for centralized jurisdiction and administration of the debtor, its estate and its reorganization in the Bankruptcy Court, and [this policy] is effectuated by Sections 362 and 105 of the Code." *In re Ionosphere Clubs*, 922 F.2d 984, 989 (2d Cir. 1990) (emphasis added, quotations and citations omitted, alterations in original). This policy of centralizing disputes in the bankruptcy court promotes judicial economy and ensures that there will not be conflicting or inconsistent judgments.

28. Here, Tide complains of "having its interests threatened in two different forums" and expressly acknowledges that "there is a risk of conflicting judicial decisions" with respect to the disposition of the Escrow Funds. Mot. ¶ 47. Puzzlingly, Tide avers that lifting the stay will address these concerns. Just the opposite is true and Tide cannot seriously claim that denying Tide's Motion while the Debtors attempt to reorganize would in any way expose Tide to the "double jeopardy" to which it vaguely alludes. By keeping the stay in place and allowing the ownership of the Escrow Funds and the dollar value of Tide's claims (both "core" issues) to be determined by this Court, Tide will not have to litigate in two different forums and the risk of inconsistent judgments will be eliminated. In this way, keeping the stay in place will promote judicial economy. Even if it were some day liquidated before the District Court or other tribunal, Tide's liquidated claim is still subject to disposition before this Court.

29. Tide also makes much of the fact that the District Court Action was filed nearly two years ago. However, as noted above, the District Court Action has barely proceeded

past the motion to dismiss phase and the matter is far from ready for trial. Judge Wood has made very few rulings in the case and there will be little, if any, duplication of judicial effort for this Court to make rulings on motions and issues that have not yet been presented to Judge Wood. In fact, denying the Motion will reduce overall judicial efforts because the Hopper Parties' pending motion to intervene in the District Court Action will be rendered moot and the need for coordination between two courts deciding related issues will be eliminated.

5. Lifting the Stay Will Prejudice Other Creditors (Seventh *Sonnax* Factor)

30. The Hopper Parties, as creditors of Falcon, believe that they have a competing claim to the Escrow funds and, therefore, that their interests are implicated by the District Court Action. The Hopper Parties filed a motion to intervene in the District Court Action and Tide filed a lengthy memorandum of law opposing the Hopper Parties' motion to intervene. *See* District Court Action Docket No. 125. The District Court Action was stayed before the court ruled on the motion to intervene and it remains unclear whether the motion would be granted.

31. In the interim, the Hopper Parties filed their Hopper Adversary proceeding in this Court asserting that a portion of the Escrow funds are not property of the Falcon estate and are not subject to the claims of Falcon's creditors, such as Tide. According to Tide, the "Hopper Adversary…cannot proceed absent resolution of the claims in the District Court Action…." Mot. ¶ 39. Although there is no legal basis for this assertion, and it actually reverses the order of the proper disposition of issues as to property of the estate, it exposes Tide's intent to block the Hopper Parties' efforts to participate in the dispute over the Escrow Funds in any court. This Court has jurisdiction over the Hopper Adversary and the ability to consolidate the core issues in all of the actions involving the property of and claims against the Debtors in "a

single organized proceeding." *In re AP Indus., Inc.*, 117 B.R. at 798 (Bankr. S.D.N.Y. 1990). This will allow all interested parties to participate in the process and will prevent Tide "from reaching the assets of the debtor's estate piecemeal." *Id.* In contrast, if the stay is lifted and Tide is able to exclude the Hopper Parties from the District Court Action, the Hopper Parties may be prejudiced. As noted below, because the other Debtors would be forced to pay Falcon's costs of defense and because litigating the District Court Action would distract the Debtors' management from their reorganization efforts, all of the Debtors' creditors will be harmed by lifting the stay.

6. The Debtors' Insurers Have Not Assumed Any Responsibility For Defending the District Court Action (Fifth *Sonnax* Factor)

32. The Debtors' insurers have not assumed any responsibility for defending the District Court Action. Accordingly, if the stay is lifted the Debtors will be forced to outlay hundreds of thousands of dollars in fees to defend the District Court Action at a time when the Debtors' cash reserves are being depleted by other administrative expenses—thereby undermining one of the key objectives of the stay. *See, e.g., Borman v. Raymark Indus., Inc.*, 946 F.2d 1031, 1036 (3d Cir. 1991) ("The automatic stay was designed …to forestall the depletion of the debtor's assets due to legal costs in defending proceedings against it….").

7. Lifting the Stay Would Harm the Debtors' Reorganization Efforts (Twelfth *Sonnax* Factor)

33. The balance of harms supports denying the Motion. In arguing that the balance of harms weighs in its favor, Tide totally fails to acknowledge the complexity surrounding the Debtors' bankruptcy cases and that the Debtors are currently in the crucial stages of their reorganization efforts. Instead, Tide focuses on the Falcon case alone and asserts that the "Falcon bankruptcy proceeding is essentially incapacitated pending a determination of ownership of the Escrow Funds because such funds are the Falcon estate's primary alleged asset…and that matter is squarely before Judge Wood in the District Court Action." Mot. ¶ 45. Besides

completely ignoring the impact of lifting the stay on the Arcapita case, Tide's assertions miss the mark. As noted previously, the question of ownership of the Escrow Funds is not before the District Court at this time. If moving that "core" issue to the District Court by lifting the stay would "essentially incapacitate[]" the Falcon case, that is all the more reason to deny the Motion.

34. As this Court is well aware, the Debtors are dealing with a number of complex and pressing bankruptcy issues. To deprive the Debtors of the protections afforded by the automatic stay at this juncture would negatively impact the Debtors by interfering with the bankruptcy process which, in turn, prejudices their creditors.

35. Tide makes only one real argument as to the harm it will allegedly suffer from allowing the Debtors to first reorganize before Tide's claims are liquidated. *See* Mot. ¶ 45.[4] Without any proof or authority, Tide contends that it will be harmed by a delay in liquidating its claims because it argues that assets of the Falcon estate will be used to pay the costs of the Debtors' reorganization generally and, therefore, Tide needs to liquidate its claims and allegedly immediately seize the Escrow Funds to prevent their dissipation. However, Falcon's assets consist almost entirely of the Escrow Funds, which have not and (without an order of this Court cannot) be spent to pay administrative or even ordinary course expenses. Monthly, this Court reviews and approves cash management orders based on a budget which discloses sources and uses of cash. Plus, the order approving the joint administration of the Falcon case requires the Debtors to give Tide separate notice regarding any disposition of funds to or from the Falcon estate. Hence, the potential harm to which Tide refers is wholly illusory.

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[4] Strangely, Tide also avers that keeping the stay in place will harm Tide because the question of the ownership of the Escrow Funds is at issue in both the Hopper Adversary and the District Court Action. Although Tide's premise is false, if the ownership of the Escrow Funds were at issue in both proceedings, the Debtors are at a loss to figure out how keeping the stay in place so that the issue is only decided in one forum harms Tide.

36. Conversely, Tide wants to force Falcon to immediately defend a complex contract and tort action and incur enormous legal fees which will presumably be paid by the estates of Debtors other than Falcon, thereby prejudicing the creditors of those estates. Or, Tide is attempting to force Falcon into litigation while at the same time denying it the ability to pay for its defense. There is no other possibility.

37. If Falcon is forced to immediately proceed with the defense of Tide's claims, then Falcon should be allowed to use the Escrow Funds to pay for its defense. If Tide in fact claims that it holds present title or other lien on the Escrow Funds that prevents Falcon's payment of its defense costs, then this Court should first resolve that core issue before any proceedings to liquidate Tide's claims.

38. Since there is no credible showing that Tide will be harmed by allowing the Debtors reorganization to proceed before Tide's claims are liquidated, at this early stage of this large and complex case, this alone is reason to deny relief from stay. In contrast, the burden imposed on the Debtors in terms of the time, financial resources, and attention necessary to defend themselves in the District Court Action far outweighs any purported harm to Tide. *See In re Calpine*, 365 B.R. 401, 413 (S.D.N.Y. 2007) ("The only way that [plaintiffs are] certain to be better off in the absence of a stay is if [they] prevail[] against [debtor] and thereby [are] able to obtain recovery sooner rather than later. The inability . . . to obtain a hypothetical recovery sooner rather than later, however, is not a harm—and is certainly not an irreparable harm—sufficient to outweigh the irreparable harm that [debtor] will suffer if the [action] were permitted to proceed."); *In re Lomas Fin. Corp.*, 117 B.R. 64, 67 (S.D.N.Y. 1990) (upholding bankruptcy court's conclusion that "it is not possible for the debtor to be a bystander to a suit which may have a $20 million issue preclusion effect against it…."; holding that debtor's reorganization

would suffer irreparable harm if creditor's suit against debtor's officers were permitted to continue); *In re Northwest Airlines Corp.*, No. 05-17930 (ALG), 2006 WL 382142, at *2 (Bankr. S.D.N.Y. Jan. 12, 2006) ("an order lifting the automatic stay would significantly prejudice the Debtors and their efforts to reorganize. . . . [Debtors] are managing a case with over 1,700 docket entries to date and have been dealing with a number of complex issues on an expedited basis").

B. The Motion is Premature

39. The automatic stay "provide[s] debtors with temporary respite from their creditors so that they may have an opportunity to develop and implement plans of reorganization to satisfy their creditors and resuscitate their businesses[]." *In re 160 Bleeker St. Assocs.*, 156 B.R. 405, 411 (S.D.N.Y. 1993). This "breathing spell" that shields debtors from creditor harassment and from a multitude of litigation in a variety of forums at a time when a debtor's personnel should be focusing on restructuring is one of the fundamental protections afforded by the Bankruptcy Code. *See, e.g., E. Refactories Co. v. Forty Eight Insulations*, 157 F.3d 169, 172 (2d Cir. 1998); *Teachers Ins. & Annuity Ass'n of Am. v. Butler*, 803 F.2d 61, 64 (2d Cir. 1986).

40. As noted above, the Debtors are laser-focused on their restructuring efforts and need a "breathing spell" from litigation to preserve the value of their estates for the benefit of all creditors. The time for litigating claims against the Debtors' estates will come in due course; but it has not yet arrived. Indeed, the bar date is still nearly a month away. Further, the treatment of unsecured claims in any plan confirmed in the Arcapita case may have a significant impact on Tide's interest in proceeding with expensive litigation against Arcapita, and Tide should wait to review any confirmed plan before proceeding. Tide should file its alleged claims and participate in the claims objection and reconciliation process with all of the other creditors that have disputed claims. If, in connection with that process, Tide thinks the stay should be lifted it could be allowed to renew its Motion to seek liquidation of its claims in the District

Court. But, at this time the Motion represents little more than an effort to jump the gun on claims litigation to the detriment of the Debtors' estates. Thus, at a minimum the Court should deny the Motion without prejudice as premature.

C. The Court Should Order the Parties to Mediation.

41. The Court should deny the Motion and before reconsidering it at a later date, at the appropriate time and before the parties engage in full scale litigation at the expense of perhaps millions of dollars in fees, the Court should order the parties to mediation. As Judge Peck observed in connection with the *Lehman Brothers* case:

> [T]he existence of the stay is not inconsistent with the pursuit of negotiations that could lead to a resolution of this ongoing dispute. … [I]t's possible for the parties to engage in potentially productive discussions, notwithstanding the fact that they [sic] stay remains in effect. To the extent that the existence of the stay is viewed as an impediment of any sort to meaningful dialogue, I want to be absolutely clear in saying that I do not believe the stay impacts in any adverse way the ability of the parties to meet and confer—to mediate or to otherwise seek a constructive resolution of the matters that are currently before the [other court].

In re Lehman Brothers Holdings, Inc., Case No. 08-13555, May 12, 2010 Hearing Transcript, at 74:4-74:19 (Bankr. S.D.N.Y. 2010).

42. In that regard, the Debtors suggest that the Court direct the parties to mediate on a reasonable schedule in an effort to resolve their disputes without judicial intervention. This approach to resolving the various claims at issue would be more efficient and less time consuming and costly than lifting the stay for the parties to resume scorched-earth litigation.

43. If mediation is unsuccessful, the Court can then address the core issues of whether the Escrowed Funds are property of the estate and, if so, whether Tide or the Hopper Parties have any lien rights or other superior rights to those funds ahead of other creditors—the

universe of which we will not know until the bar date passes and any substantive consolidation arguments are later considered.

CONCLUSION

For the reasons set forth herein, the Debtors respectfully request that the Motion be denied.

Dated: New York, New York
July 29, 2012

Respectfully submitted,

/s/ Michael A. Rosenthal
Michael A. Rosenthal (MR-7006)
Janet M. Weiss (JW-5460)
Craig H. Millet (admitted *pro hac vice*)
Matthew K. Kelsey (MK-3137)
GIBSON, DUNN & CRUTCHER LLP
200 Park Avenue
New York, New York 10166-0193
Telephone: (212) 351-4000
Facsimile: (212) 351-4035

ATTORNEYS FOR THE DEBTORS AND
DEBTORS IN POSSESSION

Exhibit A

In re Lehman Brothers Holdings, Inc., Case No. 08-13555, May 12, 2010 Hearing Transcript (Bankr. S.D.N.Y. 2010).

UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF NEW YORK

Case Nos. 08-13555(JMP); 08-01420(JMP)(SIPA)

- -x

In the Matter of:

LEHMAN BROTHERS HOLDINGS INC., et al.

Debtors.

- -x

In the Matter of:

LEHMAN BROTHERS INC.

Debtor.

- -x

United States Bankruptcy Court

One Bowling Green

New York, New York

May 12, 2010

10:07 AM

B E F O R E:

HON. JAMES M. PECK

U.S. BANKRUPTCY JUDGE

HEARING re Conference re: Alternative Dispute Resolution Procedures for Affirmative Claims of Debtors Under Derivatives Contracts

HEARING re Debtors' Motion for Authority to Compromise Controversy in Connection with a Repurchase Transaction with Fenway Capital, LLC and a Commercial Paper Program with Fenway Funding, LLC

HEARING re Motion of the SunCal Debtors for Order Determining that Automatic Stay Does Not Apply; or, in the Alternative, Relief from the Automatic Stay

HEARING re Motion of Debtors and Debtors in Possession for Entry of an Order to Consolidate Certain Proceedings and Establish Related Procedures

HEARING re Debtors’ Motion to Compel Performance by Norton Gold Fields Limited of its Obligations Under an Executory Contract and to Enforce the Automatic Stay

HEARING re LBSF v. BNY Corporate Trustee Services Ltd. [Adv. Case No. 09-01242] - Status Conference re Motion and Memorandum of Law of Defendant BNY Corporate Trustee Services Limited in Support of its Motion for Entry of an Order, or, Alternatively, to Reopen and Reargue the Parties' Cross-Motions for Summary Judgment

HEARING re Neuberger Berman v. PNC Bank, NA, et al. [Case No. 09-01258] - Status Conference re COMPLAINT FOR INTERPLEADER

Transcribed by: Lisa Bar-Leib

A P P E A R A N C E S :

WEIL, GOTSHAL & MANGES LLP
Attorneys for Debtor and Debtors-in-Possession
767 Fifth Avenue
New York, NY 10153

BY: PETER GRUENBERGER, ESQ.
RICHARD W. SLACK, ESQ.

WEIL, GOTSHAL & MANGES LLP
Attorneys for Debtor and Debtors-in-Possession
700 Louisiana
Suite 1600
Houston, TX 77002

BY: ALFREDO R. PEREZ, ESQ.

WEIL, GOTSHAL & MANGES LLP
Attorneys for Debtor and Debtors-in-Possession
1300 Eye Street, N.W.
Suite 900
Washington, DC 20005

BY: RALPH I. MILLER, ESQ.

JONES DAY
Special Counsel for the Debtors
222 East 41st Street
New York, NY 10017

BY: JAYANT W. TAMBE, ESQ.
AVIVA W. SISITSKY, ESQ.

MILBANK, TWEED, HADLEY & MCCLOY LLP
Attorneys for Official Committee of Unsecured Creditors
One Chase Manhattan Plaza
New York, NY 10005

BY: EVAN R. FLECK, ESQ.
DENNIS C. O'DONNELL, ESQ.

MILBANK, TWEED, HADLEY & MCCLOY LLP
Attorneys for Official Committee of Unsecured Creditors
International Square Building
1850 K Street, NW
Washington, DC 20006

BY: DAVID S. COHEN, ESQ.
WILBUR FOSTER, ESQ.

HUGHES HUBBARD & REED LLP
Attorneys for SIPA Trustee
One Battery Park Place
New York, NY 10004

BY: JEFFREY S. MARGOLIN, ESQ.

U.S. DEPARTMENT OF JUSTICE
Office of the United States Trustee
33 Whitehall Street
21st Floor
New York, NY 10004

BY: ANDREW D. VELEZ-RIVERO, ESQ.

BUCHANAN INGERSOLL & ROONEY PC
Attorneys for PNC Bank, National Association
One Oxford Centre
20th Floor
301 Grant Street
Pittsburgh, PA 15219

BY: KATHLEEN J. GOLDMAN, ESQ.

DEWEY & LEBOEUF LLP
Attorneys for Fenway Capital and Fenway Funds
1301 Avenue of the Americas
New York, NY 10019

BY: RICHARD W. REINTHALER, ESQ.
IRENA M. GOLDSTEIN, ESQ.

GIBSON DUNN & CRUTCHER LLP
Attorneys for BNY Corporate Trustee Services Limited
200 Park Avenue
4th Floor
New York, NY 10166

BY: RANDY M. MASTRO, ESQ.

MILLER BARONDESS, LLP
Special Litigation Counsel for SunCal Debtors
1999 Avenue of the Stars
Suite 1000
Los Angeles, CA 90067

BY: LOUIS R. MILLER, ESQ.
MARTIN H. PRITIKIN, ESQ.

REED SMITH LLP
Attorneys for BNY Corporate Trustee Services Limited
599 Lexington Avenue
New York, NY 10022

BY: ERIC A. SCHAFFER, ESQ.

SHEARMAN & STERLING LLP
Attorneys for Nomura International plc and Nomura Securities Co., Ltd.
599 Lexington Avenue
New York, NY 10022

BY: DOUGLAS P. BARTNER, ESQ.
SOLOMON J. NOH, ESQ.
DANIEL LEWIS, ESQ.

SHEPPARD MULLIN RICHTER & HAMPTON, LLP
Attorneys for Norton Gold Fields Limited
30 Rockefeller Plaza
24th Floor
New York, NY 10112

BY: EDWARD H. TILLINGHAST, III, ESQ.
BLANKA K. WOLFE, ESQ.

STROOCK & STROOCK & LAVAL LLP
Attorneys for Neuberger Berman Management, LLC
180 Maiden Lane
New York, NY 10038

BY: BENJAMIN I. RUBINSTEIN, ESQ.

WHITE & CASE LLP
Attorneys for the Ad Hoc Group of Lehman Brothers Creditors
1155 Avenue of the Americas
New York, NY 10036

BY: GERARD UZZI, ESQ.

WINTHROP COUCHOT PROFESSIONAL CORPORATION
Attorneys for the SunCal Voluntary Debtors
660 Newport Center Drive
Fourth Floor
Newport Beach, CA 92660

BY: SEAN A. O'KEEFE, ESQ.
PAUL J. COUCHOT, ESQ. (TELEPHONICALLY)

BROWN RUDNICK LLP

Attorneys for Ad Hoc Group of Lehman Brothers Creditors

One Financial Center

Boston, MA 02111

BY: ANGELO THALASSINOS, ESQ.

(TELEPHONICALLY)

CHAPMAN & CUTLER LLP

Attorneys for U.S. Bank

111 West Monroe Street

Chicago, IL 60603

BY: JAMES HEISER, ESQ.

FRANKLIN H. TOP III, ESQ.

(TELEPHONICALLY)

CLEARY GOTTLIEB STEEN & HAMILTON LLP

Attorneys for Goldman Sachs Bank, USA and Goldman Sachs International

2000 Pennsylvania Avenue, NW

Washington, DC 20006

BY: BENJAMIN MEEKS, ESQ.

(TELEPHONICALLY)

IRELL & MANELLA LLP

Attorneys for Official Committee of Unsecured Creditors

840 Newport Center Drive

Suite 400

Newport Beach, CA 92660

BY: ALAN J. FRIEDMAN, ESQ.

(TELEPHONICALLY)

LEO & WEBER, P.C.
Attorneys for Liberty Mutual
One N. LaSalle Street
Suite 3600
Chicago, IL 60602

BY: T. SCOTT LEO, ESQ.
(TELEPHONICALLY)

MILLER STARR & REGALIA PLC
Attorneys for Miller Starr & Regalia
1331 North California Boulevard
Walnut Creek, CA 94596

BY: TARA C. NARAYANAN, ESQ.
(TELEPHONICALLY)

PACHULSKI STANG ZIEHL & JONES LLP
Special Counsel to the Debtors and Debtors-in-Possession
10100 Santa Monica Boulevard
11th Floor
Los Angeles, CA 90067

BY: DEAN A. ZIEHL, ESQ.
(TELEPHONICALLY)

STUTMAN TREISTER & GLATT LLP
Attorneys for Perry Capital
1901 Avenue of the Stars
12th Floor
Los Angeles, CA 90067

BY: MARINA FINEMAN, ESQ.
JEFFREY H. DAVIDSON, ESQ.
WHITMAN L. HOLT, ESQ.
(TELEPHONICALLY)

P R O C E E D I N G S

THE COURT: Be seated, please. Well, you're in the position to give a report.

MR. GRUENBERGER: Yes, Your Honor. Good morning.

THE COURT: Good morning.

MR. GRUENBERGER: Peter Gruenberger, Weil Gotshal & Manges for the debtors. May it please the Court. I'll be very brief. We are here today regarding Your Honor's ADR procedures order that governs debtors' affirmative claims under derivatives contracts with counterparties. And particularly, paragraph 10 of that order which requires that a monthly report be submitted to Your Honor giving a scorecard of how we're doing.

Your Honor issued that order on September 17, 2009. It took a few weeks to get going but we've been in full swing now for about six months. We and the creditors' committee concurred that with this six-monthly report that I submitted yesterday, we would put it on the docket so all interested parties could see the progress that we were making in this effort.

As the report to you demonstrates, the process is very much alive and healthy as we both predicted back in September when you signed the order. As of yesterday, forty-five ADR notices were served on seventy-one different counterparties. We had achieved as of yesterday ten settlements, four after-

mediations and six pre-mediations in the ADR process. Had I waited two more hours, we could have added another success to that scorecard because the fifth mediation came through with a settlement. So now we're batting one thousand, five of five in mediations and have eleven settlements involving fifteen counterparties.

So we have added to date thirty-nine million new dollars to the treasury of the debtors' estates for the benefit of all creditors. And we are going strong. We have eight more mediations scheduled over the next six weeks. And we will report monthly. And I would hope that we could, every six months perhaps, post the status report on the docket and make a report to Your Honor, if that's okay.

THE COURT: I appreciate that. Let me just ask you this question.

MR. GRUENBERGER: Certainly.

THE COURT: Obviously, the successful outcomes speak for themselves. But in terms of procedure, is the ADR procedure working well in terms of efficiency and are there any areas needing improvement?

MR. GRUENBERGER: I would say, overall, it's very efficient. There are some bumpy spots where parties, especially parties in different parts of the world cannot communicate as quickly as one would like in a perfect world, but it's not a perfect world. And so we ride with those bumps.

and we overcome the hurdles. The mediators are working hard. The creditors committee and we are getting along well. And I see no gross inefficiencies whatever. I think that maybe over the next six months I can report more fully but there's no complaints out of any court from anyone.

THE COURT: Good. I appreciate that. Is there anyone else who wishes to be heard on this subject? Fine.

MR. GRUENBERGER: Thank you.

THE COURT: Let's move on to the next part. And, Mr. Gruenberger, if you wish to be excused, you may be; if you wish to stay, you're welcome to stay.

MR. GRUENBERGER: Thank you, Your Honor.

MR. PEREZ: Good morning, Your Honor. Alfredo Perez on behalf of the debtors. And I'm here on the debtors' motion for authority to compromise with Fenway, docket number 7831. May I proceed?

THE COURT: Sure.

MR. PEREZ: Your Honor, this is a 9019 motion in which LCPI and LBHI seek -- on the one hand, seek to compromise and, basically, do away with the Fenway structure. And it involves a settlement with Fenway, Fenway Funding -- Fenway Capital and Fenway Funding, Hudson Castle and the trustee or the administrator which is Deutsche Bank.

Your Honor, we have received one objection to it from the SunCal debtors. Both the unsecured creditors' committee

has filed statements in support as has Fenway.

Your Honor, last night, we received and was filed on the record a withdrawal of the objection on behalf of the SunCal involuntary debtors. I don't know if the Court's aware of that.

THE COURT: I'm aware of it but I'm not sure if it was a withdrawal on behalf of the SunCal voluntary debtors or the trustee.

MR. PEREZ: The trustee, Your Honor. It's the -

THE COURT: It was from Lobel.

MR. PEREZ: From Mr. Lobel. It's on behalf of the trustee.

THE COURT: I didn't understand it because it was a withdrawal without prejudice. I don't know what that means.

MR. PEREZ: Well, Your Honor, I think what that means is that the debtors and the trustee are in the process of documenting a settlement that would resolve all the disputes between the Lehman debtors and the trustee. And the key fact about that, Your Honor, is that the property which the trustee controls is about seventy-five percent of the value of the SunCal debtors. So we're talking about we're on the verge of finalizing and documenting a settlement with the party that has the vast majority of the SunCal assets.

THE COURT: All right.

MR. PEREZ: So -- and not --

THE COURT: Let me just ask if the trustee is represented in court today or on the telephone.

(Pause)

THE COURT: Apparently, yes.

MR. O'KEEFE: Actually, Your Honor, I represent the voluntary SunCal debtors.

THE COURT: You represent --

MR. O'KEEFE: The voluntary SunCal debtors not the involuntary debtors, although I could speak to the issue from a knowledge perspective but not on behalf of the trustee.

THE COURT: All right. So there's no one here acting as local counsel for Mr. Lobel and Mr. Lobel is not on the phone?

MR. O'KEEFE: Not to my knowledge, Your Honor.

THE COURT: Okay. Why don't you proceed?

MR. PEREZ: Thank you, Your Honor. So, Your Honor, I think this is a key development not only as it relates to this motion but, absolutely, as it relates to the motion of lift stay because they've also withdrawn their request on the motion to lift stay.

So, Your Honor, what we have is a situation where -- and Fenway has obviously been the subject of a lot of scrutiny recently. But it's a structure whereby LCPI repo'd certain assets to Fenway. Fenway then, in turn, issued a commercial paper note that was purchased by LBHI. I have a chart. It's

similar to the chart that was attached to one of the pleadings, Your Honor. If I may approach?

THE COURT: Sure. Thank you.

MR. PEREZ: But, in essence, Your Honor, it's a very simple chart. LCPI repo'd the assets to Fenway Capital. Fenway Capital issued a variable funding note to Fenway Funding. Fenway Funding then issued commercial paper. That commercial paper was purchased by LBHI. Approximately three billion dollars. Those -- that commercial paper was pledged to JPMorgan. And, Your Honor, the reason we can undo the structure currently is because as a result of the JPM agreement, the CDA, we now have -- LBHI now has that commercial paper.

So the goal, Your Honor, is to reduce the cost associated with the Fenway structure, be able to deal with the assets directly. SunCal is about half of the three billion in Fenway assets. In connection with that, there are other assets, some of them not even real estate related, that sit in the Fenway structure that LCPI and LBHI need to deal with.

THE COURT: What's the Hudson Castle involvement with this?

MR. PEREZ: Your Honor, Hudson Castle -- and Ms. Goldstein is here and could address this. But Hudson Castle is basically the manager of the Fenway structure, Your Honor.

So, to some extent, what we've done here is just a

plain vanilla motion which seeks to not only undo the structure but, very critically, maintain the status quo among the debtors. That's a critical importance. As the Court is aware, we filed twenty-three separate plans. I mean, one document but twenty-three separate plans. The recovery percentages for the LBHI creditors are different than the recovery percentages for the LCPI creditors. So we do not want to, in any way, shape or form, affect what the recovery balances would be. And in connection with that, in the motion as filed, we indicated that LBHI would be tendering the commercial paper notes as the guarantor, 'cause LBHI was on both sides, not only did it buy the commercial paper but it also guarantied LCPI's obligations under the Master Repurchase Agreement. So they tendered as the guarantor. They tendered the notes as the guarantor. And there was a full reservation of rights as between the debtors to make sure that we could allocate the value as was indicated. Subsequent to that, there were -- this was filed on March -- mid-March. The JPMorgan agreement was approved, I think, either shortly thereafter or right around the time we filed it at the March hearing. Since that time, a bunch of time has passed. We have further refined the reservation of rights to make sure that we maintain the rights as between the parties. So we filed the supplemental order, the revised order, which made sure that everybody maintained their rights. And then we also filed a supplement to the motion. And basically, what the

supplement did was, at the time that we originally structured the transaction, Fenway and Hudson Castle were getting limited releases. Deutsche Bank was getting a full release. Through the supplement to the motion, those releases were further scaled back -- the releases that Fenway and Hudson Castle were getting were further scaled back. So that's the purpose of those two motions.

Now, Your Honor, as I read -- and there's been a lot of paper filed. But as I read the papers, there's really no objection to the debtors' business judgment in doing this transaction. I mean, we're going to be saving costs, we're getting rid of structure. We're going to be able to deal with the assets directly. I think the objections go to other things, not really related to the business judgment.

I have Mr. Fitts here who could talk to the business judgment. I don't think that's really necessary to put him on because we just really -- there's no allegation that there is any -- that we're not exercising our business judgment.

The focus is whether this is being done somehow in bad faith. And, Your Honor, I submit there's absolutely no evidence that this is being done in bad faith. I --

THE COURT: Well, consistent with the fact that we have a contested hearing still on this, you might want to proffer the testimony that you have available, both as it relates to the purpose of the transaction and the good faith of

the transaction and why it's being done now.

MR. PEREZ: Yes, Your Honor. I could certainly do that. Your Honor, Mr. Fitts is in the courtroom. I believe he's testified before. As the Court is aware, Mr. Fitts is a managing director with Alvarez & Marsal. He is the co-head of the real estate group at Lehman and he's familiar with this transaction. He was managing director at GE and was formerly in Citibank's workout group where he had extensive experience since approximately 1988.

He's been assigned to the representation of Lehman since September of 2008. In connection with the Fenway repo and the Fenway commercial paper program, he has reviewed the motion and informed himself of the relevant transaction as embodied in the various documents.

He would testify that the assets were repo'd to Fenway and that the goal of this motion is to be able to save the money that's associated with maintaining the structure; that in September of 2008, Fenway Funding issued commercial paper notes to LBHI and that LBHI is the current holder of those notes; that the proposed actions are intended to eliminate the expense and time delay associating with maintaining the programs; eliminating the administrative fees to Deutsche Bank, Hudson Castle and other third parties in connection with maintaining the repo and the commercial program; and enabling LBHI to access certain funds that are currently held at the Fenway

structure in approximately a little over a million dollars.

He would testify that the transaction is done on the basis of arm's length negotiation with Fenway and that the goal would be to put LCPI in the position that it was prior to the time of the funding of the repo maintaining LBHI's interest in the notes.

Additionally, Your Honor, Mr. Fitts would testify that as a result of the transaction with JPMorgan Chase that we're able to undo the structure and that there are several other structures that hold real estate assets that now, as a result of the JPMorgan transaction are in the process of being unwound.

Mr. Fitts would further testify that this is a reasonable exercise of the debtors' business judgment to alleviate the expense and time delay associated with maintaining both the repo and the commercial paper program; that it was done -- that the transaction is fair and reasonable to the debtors under the circumstances; and that it was the product of protracted arm's length negotiation.

LBHI would indemnify Fenway and Hudson Castle with respect to certain activities related to the assets as modified by the supplement to the carve-out of the indemnity and the guaranty. In addition, they would pay approximately a million six in attorneys' fees to Fenway in connection with the amounts of money that they have expended.

Mr. Fitts would further testify that the concessions that have been made by LBHI and LCPI are far outweighed by the benefits that LBHI and LCPI would receive as a result of undoing the structure.

Your Honor, I don't think -- that would be the conclusion of his testimony.

THE COURT: Is there any objection to my receiving the proffer in evidence in support of the motion?

MR. O'KEEFE: Good morning, Your Honor. Sean O'Keefe appearing on behalf of the voluntary SunCal debtors. My only objection is to the extent that the testimony, counsel's characterization of testimony is inconsistent with what is reflected in the motion then I would seek the right to cross-examine Mr. Fitts because the characterization by counsel of certain elements of that transaction is directly contrary to what is reflected in the motion. And if that's the testimony then I would respectfully ask the Court to have Mr. Fitts take the stand on those limited issues.

THE COURT: If you wish to cross-examine, that's your right.

MR. O'KEEFE: Then I would ask the Court to call him to the stand.

MR. PEREZ: Your Honor, I'm not sure that anything in his testimony contradicted what's in the motion or what's in the transaction. And, frankly, Your Honor, this is a common

theme in their objection which I, frankly, don't understand. It's our motion with Fenway. We can basically file a motion requesting for the Court to do various things. I'm not sure I understand what the objection is. I think we've clearly reflected what we want the motion to do, that we want it to preserve the integrity as between LCPI and LBHI. So I'm not sure what the nature of the objection is.

MR. O'KEEFE: Your Honor --

THE COURT: Well, at the moment, we're dealing with a very limited question which is whether the proffer of Mr. Fitts' testimony is to be accepted as is or whether or not you want the right to cross-examine. You have the right to cross-examine as an objector regardless of your rationale. And if you want to have Mr. Fitts on the stand, ask him some questions, he's here. So we can have him come to the stand. We don't have to have an argument about whether or not you have some basic right to object. You do. It doesn't matter what your objection is. You're a party in interest; you're objecting. I think I know what your objection's about. It's about having these loans come into the estate and be subject to the automatic stay and the SunCal litigation in California. Isn't that right?

MR. O'KEEFE: Your Honor, certainly that is our primary concern. And just to respond to counsel's comment, I, in no way, want to interfere with this transaction except in

the following limited respect. I understand --

THE COURT: Well, that means you do want to interfere the transaction.

MR. O'KEEFE: Well, Your Honor, not as stated in the motion. Not as stated in the motion. The motion states, "The parties will terminate the MRA". So the MRA is terminated. So this contention that a terminated contract can somehow give rise to liens which are provided for therein, that would be my issue. So if they're saying it's not terminated, that's not what' s in their motion. They say the guaranty will be terminated. So we would simply ask them to acknowledge the guaranty is terminated. And that's the basis for their claims against LCPI. They also state the CP notes are terminated. That's right here in front of me on page 10. "The CP notes are terminated." This exchange, they state, is in full payment of the purchase price under the MRA. So that transaction is done; it's over. I think we can all agree you can't have a lien if there's no claim. You can't have a lien if there's no underlying lien documents.

THE COURT: Well, we're not arguing your objection right now. We're dealing with, as I said, a very narrow question. Do you want to examine Mr. Fitts? If so, we'll call him to the stand now. If you want to accept the proffer, we can accept the proffer with your rights reserved in terms of what you're arguing about and we can reserve that to argument.

But that's what's currently in front of me.

MR. O'KEEFE: Well --

THE COURT: It's binary. We either have Mr. Fitts or we don't have Mr. Fitts as a witness.

MR. O'KEEFE: Your Honor, then we would -- we would reserve our rights. The only issue is I have a material concern about Your Honor making findings based upon that characterization of the testimony as opposed to what is before us in terms of their motion.

THE COURT: Well, you can certainly argue whatever you want to argue about the reasonable conclusions to be drawn from the record. And you're also free, if you wish, to call Mr. Fitts to the stand and ask him as many direct questions as you wish.

MR. O'KEEFE: Your Honor --

THE COURT: If you want to simply reserve this to argument, that's fine, too. It's up to you.

MR. O'KEEFE: We will reserve it, Your Honor. We understand the standard. I agree they have a lot of discretion. And we're certainly not here to interfere with this transaction. We're not a claimant in this case. So we haven't asserted standing to get into the issue of the merits.

THE COURT: Oh. Then why don't you just sit down?

MR. O'KEEFE: I will, Your Honor.

THE COURT: If you acknowledge you don't have

standing --

MR. O'KEEFE: Only in terms of the issue of their discretion and that transaction. But to the extent that those -- the assertion of those findings relative to the characterization of the transaction could affect my client then I did have concerns. And Your Honor is saying that you're inclined to approve the transaction, as I understand it, without making those findings.

THE COURT: No. I didn't say that. What I said was that if you have a concern about the proffer and wish to examine the witness in order to make a record that you view to be either more consistent with your understanding of the facts or more helpful to you in the argument you wish to make when we get into the legal argument phase of this, you're free to call the witness. That's the only thing we're talking about now.

MR. O'KEEFE: Very well, Your Honor. We will reserve the right for the following motion.

THE COURT: All right. So I take that as you're not calling Mr. Fitts. I don't have any questions of Mr. Fitts. I accept the proffer with such conclusions to be drawn from the proffer as will be determined following argument.

MR. O'KEEFE: Thank you, Your Honor.

THE COURT: Okay.

MR. PEREZ: Your Honor, I'm glad Mr. O'Keefe brought up the question of standing. And the only reason I raise it is

because I did -- I'm kind of a newcomer to this whole situation. So I did look up to see if there had been any proofs of claim filed. I couldn't find any proofs of claim that had been filed by any of the SunCal debtors one way or another. So obviously, they filed a motion to lift stay. But I haven't been able to determine, in fact, what their standing is. And they certainly haven't filed a proof of claim in this proceeding.

(Pause)

MR. PEREZ: Just to continue, Your Honor, as it relates to the indication of bad faith, the committee has reviewed this transaction, has reviewed this transaction extensively. They have filed two documents in support of the transaction. There's no indication that there's bad faith. The testimony is that this has been subject of a long negotiation, arm's length negotiation with Fenway.

So, Your Honor, the main issue that has been raised by SunCal and what I think they simply ignore at every turn and for some reason it's a little bit of "gotcha" lawyering is that LCPI has always had the right to repurchase the loans. LBHI has always been the guarantor of the loans. LBHI has always held the commercial paper which is the economic -- which is part of the economic interest in the loan. Now that it's not subject to the JPMorgan pledge, they can deal with it. There has -- Fenway has consistently taken the position -- and I

think there are five instances that were cited in the papers where they've said we're just the middleman in this. We really don't have an economic interest because you have LCPI and LBHI on one side and LBHI on the other side.

So, Your Honor, when you boil this down to its essence, two things are happening. We're doing away with a costly structure, that is Fenway. We're doing away with that and it's not the only one that we're going to be doing away with because there were several of these. Second, we are doing everything possible, as is our fiduciary obligation in connection with the representation of twenty-three separate estates to maintain the economics of each -- the integrity of the economics of each debtor. And in this case, LBHI paid for the commercial paper. They're the holder of the commercial paper. And they clearly will have an interest in those assets because those assets form part of the recovery in their estate.

So, Your Honor, I would request that the Court approve the motion. There's really been no -- no challenge to the debtors' business judgment. And I don't think there can be any real challenge to any bad faith associated with undoing this transaction. This has been going on for a long time. We have e-mails from Ms. Goldstein going back to January saying they've been wanting to get out -- and earlier, saying they've been wanting to get out of this. I mean, much longer, saying that they've been wanting to get out of the transaction. This is a

cost saving measure and it effectively allows the debtors to deal with the assets. And half of the loans in Fenway have nothing to do with SunCal, Your Honor.

THE COURT: Mr. Perez, you said a little earlier in your presentation that you're new to this.

MR. PEREZ: Correct.

THE COURT: Now, you're not new to the bankruptcy case itself, obviously. You've been involved from the very beginning.

MR. PEREZ: I have, Your Honor.

THE COURT: When you say you're new to this, do you mean you're new to the ongoing hostilities between the SunCal debtors and the Lehman estates?

MR. PEREZ: Correct, Your Honor.

THE COURT: All right. To the extent that there is an allegation of bad faith in this transaction, it seems to me that it relates to the following. There is the suggestion by the SunCal debtors that one of the motivations for this transactions is to bring assets into the debtors' estates that are not now within the estate directly by virtue of the Fenway structure, and as a result, to have those assets subject to the automatic stay which would, in their view -- and I'm characterizing their view -- materially interfere with the prosecution of equitable subordination litigation pending in the bankruptcy court in Santa Ana, California. That's my

understanding of their view as to why this transaction may be suspect. What's your response to that?

MR. PEREZ: Your Honor, I have several responses to that. First of all, that is based on what I believe to be a false premise. LCPI has always had rights to those assets through the repurchase agreement. They've always had that right. If the Court looks at the Palmdale decision while the BAP panel never reached that issue because, remember, Your Honor, there are loans that LCPI has that are not in Fenway, that are SunCal loans. So we'll get to the issue of the automatic stay at the next hearing. But there are loans in SunCal -- SunCal loans that are not in Fenway. So while the BAP never reached that decision, it did say that LCPI might likely have an interest through the repurchase agreement. That's number one.

Number two, I think that the examiner's report is fully replete with references to the fact that these repo agreements were financings, that they were not sales. I mean, that Lehman used the repo transaction in order to provide financings.

Third, Your Honor, LBHI has always had an interest. They're the ones that paid three billion dollars. They've always had an interest in these assets. They've never not had that interest.

THE COURT: I understand all that and I accept that

argument. But they're saying that this is, in part, an effort to expand the scope of the automatic stay and the SunCal litigation to these assets. And they say that various statements were made on the record that ignore the Fenway structure. It was, if I'm understanding it correctly, representations made that there was property of the estate in the SunCal bankruptcy cases when, in fact, some of loans were within the Fenway structure. And to the extent that that's true, and I'm not saying that it is true because I don't know those facts, but undoing the structure is a way to cure that defect.

MR. PEREZ: Well, Your Honor, I'm not sure that I agree with that premise. I believe that -- and I haven't gone back and read every single transcript. I've certainly read most of the stuff that's been filed. But, Your Honor, to the extent that Lehman held these assets as loans on their books, even though they were repo'd to Fenway then I think that they would have every right to do that. And every indication based on the examiner's report, that's, in fact, what they did. So I'm not sure that there is any real deception that went on there.

Furthermore, Your Honor, let me make two other points. The principal objector with seventy-five percent of the value has now stopped objecting. So we're really talking only about the smaller part of the claims. And, Your Honor, to the extent

that the Court somehow believes that there's some merit to that argument, which I don't believe there is --

THE COURT: I'm not suggesting --

MR. PEREZ: Okay.

THE COURT: -- that there is or there isn't. All I'm saying is that you're trying to get over the hurdle of this is in good faith. And one of the issues that you haven't really dealt with directly is what I've been talking about which is my characterization -- and I may have it wrong, by the way -- my characterization of what I believe to be embedded in the SunCal papers, namely, this is a device to improve Lehman's litigation position in California and that that may be one of the principal motivations for doing this deal.

MR. PEREZ: Your Honor, if as a result -- let me put it this way. If as a result of undoing the structure, the ownership of the assets is cleared up, then I think that's a salutary effect. I can't believe that would be in bad faith.

THE COURT: Okay.

MR. PEREZ: I mean, if as a result of doing the structure it's cleaned up, I can't understand why that would be in bad faith. What is it that it's in bad faith about? That's what I don't seem to understand.

THE COURT: All right. I think it's time to hear from the SunCal debtors and understand exactly from them what the problem is, if any.

And you speak softly and we have a fairly crowded courtroom. If you could -- you're close to me and I can hear you but please speak up so that everybody can hear you.

MR. O'KEEFE: Yes, Your Honor. Let me deal briefly with a few of counsel's comments. As far as Article III standing, you don't have to file a claim to have Article III standing. The reality is to the extent that what they're doing has an adverse effect on our case then we have standing to make an objection. Now, we have limited our issue to that part that affects our case.

And let me just tell you the sequence of events here that led us to the conclusion. And each sequential filing in this case has confirmed that fact. The transaction before the Court specifically states that the MRA, the master repurchase agreement, is being terminated. And just to step back from that, every repo from an economic perspective is, in effect, a secured transaction. It's a buy and sell that generates a yield between the buyer and seller. But the simple fact is that is an incredibly important market. That's how we move M1 and M2 on the money supply. So decisions were made twenty years ago that when they say it's a true sale, no matter what it looks like, it's a true sale. And this particular contract says it is a true sale. And there's twenty years of case law that says no matter what it looks like it's a true sale because that market says it's a true sale --

THE COURT: We are not arguing in the context of this motion to unwind the Fenway structure whether or not repos that function as financings are true sales. And the question that you are asserting has not been decided in this case and is not being decided now.

MR. O'KEEFE: Well, let me just deal with the issue of this transaction. The transaction in the motion says that the master repurchase agreement is being terminated. That's where the backup lien rights were vested in Fenway. And basically, the contract says this is a true sale but if for any reason it's broken, we continue to have a lien right to protect ourselves in the same way as you have a lessor saying that in a lease.

But the contract before Your Honor -- the motion before Your Honor says that contract is being extinguished. It says the guaranty that Lehman Brothers issued in favor of LCPI to back up their repurchase obligation is being extinguished. It says that the CP notes are being extinguished. It says that the VFN, or the variable funding note, is being extinguished. Every element of that transaction is being extinguished. And it says this is in full performance.

Now, we then see in the pleading and in subsequent pleadings, the development of the following argument. Notwithstanding the fact that the guaranty goes away, there's a subrogation based upon an extinguished guaranty.

Notwithstanding the fact that the MRA is gone, we say there's a lien that they're taking based on the MRA against the sold loans that are being acquired by LCPI. Transactionally, it doesn't make any sense. We then point out in our papers, wait a minute here. There is no reference to a financing -- a 364 financing in this motion. But you're referencing debt that LCPI is purporting incurring and liens that it's purporting giving to secure a debt which is not referenced in the motion. So when you see the sequence of events, they then file a supplement and said, oh well, notwithstanding the fact what we said in the motion, we're reserving rights and somehow or another there are these follow on liens which weren't discussed or could survive under the transaction that we've enunciated before the Court.

So at that point, it confirmed what was initially a suspicion. And now they've admitted that they will assert that Lehman Brothers stay a party that has -- doesn't own the loans, has never owned the loans, has never had a lien on the loans, will now acquire a lien based upon an extinguished contract, based upon a guaranty that's extinguished, based upon a transaction that is fully performed and paid.

So when we look at that sequence of events, we see that there appears to be an underlying objective to insert LBHI into a transaction and to create lien rights that really can have no existence under the transaction that they presented

before the Court.

So SunCal's objective is simply to do its own reorganization. And I'll address this in the next motion. We don't, in any way, want to get involved in Lehman's case. We haven't filed a claim. We haven't appeared here except as necessary. But when someone files a motion that presents what appears to be a clear --

THE COURT: By the way, one of the issues here is that you haven't appeared here enough, that you chose to absent yourself in Santa Ana taking actions that were, as confirmed by the BAP panel, in violation of the stay. So maybe one of the problems is you haven't been here enough.

MR. O'KEEFE: Well, Your Honor, I'm more than willing to address that, Your Honor.

THE COURT: No. You don't need to. It's an aside. But I'm not going to let an aside like that go without comment. Just finish your argument.

MR. O'KEEFE: My point, Your Honor, is the motion describes a transaction for the extinguishment of the MRA, for the extinguishment of the underlying transaction so that there would be no basis for a follow on lien by LBHI. So our concern was they were designing this to get back into the SunCal cases in California. And on that basis, we objected.

Insofar as the issue of counsel's characterization of a tentative settlement that's reached with the trustee debtors,

seventy-five percent of the value, obviously, there's no evidence before the Court with respect to that. What I would say --

THE COURT: The evidence is the withdrawal of their objection. They've withdrawn their objection and did so last evening. And I accept the representation of counsel that discussions are underway. Those are not before the Court. The only thing that's happened is that you're now the lone objector.

MR. O'KEEFE: Well, Your Honor, it's -- I think it's -- the voluntary debtors are the loan objectors. And as we'll deal with in the next motion, the reason why that settlement was possible is because of the pursuit of litigation in California, but for that --

THE COURT: That's not before me right now. The question before me -- and I understand some of what you're arguing. But I will tell you that some of what you've said I find confusing. I don't believe that there is anything in the motion before me that requires me to make any findings as to the consequences in the SunCal bankruptcy of my unwinding the structure. So part of what I don't understand is why you're spending all this time arguing about those consequences.

MR. O'KEEFE: Your Honor, with that characterization, I'm more than willing to sit down. I just wanted to make sure, Your Honor, that in connection with the next motion, I didn't

prejudice any rights in this motion. Otherwise, I wouldn't have said anything. But I appreciate Your Honor's clarification in that regard.

THE COURT: Okay. I might -- let me ask Mr. Perez, have I said it correctly? Is it correct that there's nothing about my unwinding the Fenway structure in accordance with the amended order that you have proposed that necessarily impacts the characterization of anything in the SunCal bankruptcy case?

MR. PEREZ: Your Honor, I think that's correct, Your Honor. I believe the -- once the transaction is unwound, we'll be in a position -- we'll be in the position that we find ourselves. But I don't think you're making any finding with respect to the SunCal and what our position is in the SunCal case.

THE COURT: All right. With that clarification, maybe the objection for the time being fades away. And I think it's time to hear from the creditors' committee particularly as it relates to their review of the transaction and their reservation of rights with respect to certain parties, notably, Hudson Castle and the Fenway parties.

MR. O'DONNELL: Yes, Your Honor. Dennis O'Donnell, Milbank Tweed Hadley & McCloy on behalf of the official creditors' committee. Your Honor, as Mr. Perez said, we have spent a lot of time with this motion on several different levels. Just as a preliminary matter, in terms of business

judgment, we think that -- we're totally convinced that the business judgment of the debtors here makes sense.

There are, I think, two business purposes. One is to simply making the management of the loans easier. I mean, we can speak to that from the context of transactions we've been involved in with respect to Fenway loans where the extra level of having Fenway involved made things much more complicated and time consuming. So there is that business purpose.

The second business purpose is simply to confirm the ownership of these loans in LCPI which is significant for lots of purposes, one of which might have some consequence in the SunCal proceeding, but it has other purposes as well. So to the extent we're looking for a business purpose here, there are several fairly compelling business purposes separate and apart from whatever the SunCal debtors have to say.

We did look at the motion on other levels as well. And our particular focus from the get-go was on the actual nature and structure of the transaction and the parties involved. And specifically, the involvement of Hudson Castle. Even before the audit call that appeared in the Times a few weeks ago appeared, we had been asking questions about the nature of the transaction, the intents of the transaction, how it was put together, how it unfolded. That article provoked us to look even harder at that relationship. And subsequent to that, we spent a two-week period talking to the debtors and

talking directly to Hudson Castle and its counsel trying to get a better understanding of the relationship between Hudson Castle and Lehman and precisely how the Fenway structure was put together and modified over the summer of '08.

That investigation is ongoing. We haven't had all our questions answered yet. But the ones we have answered have convinced us that we have no reason to oppose the current motion. And that's the case because the releases provided to Fenway and Hudson Castle in this motion are very limited. We had already started the process of limiting those releases. But subsequent to further investigation, we narrowed them further. And all that's getting released at this point is any claims arising out of -- and Ms. Goldstein can correct me if I'm incorrect on this -- but, basically speaking, not the specific language, any claims arising out of the administration or management or origination of the underlying loan collateral -- which we believe Hudson Castle likely had nothing to do with. All claims relating to the actual structure of the Fenway transaction and Hudson Castle's involvement in it are being preserved for future investigation. And with that understanding and our understanding and acceptance of the business judgment here, we believe the motion should be granted by the Court.

THE COURT: All right. Thank you. Is there anyone else who wishes to be heard in connection with this?

MR. MILLER: Good morning, Your Honor. I'll be very brief. My name is Skip Miller. I'm the litigation attorney for the SunCal debtors. I, obviously -- and I'm not a bankruptcy lawyer. I obviously don't want my lawsuit, my equitable subordination lawsuit encumbered or made any more difficult than it already is by virtue of this compromise motion. That's my only concern. The exact questions that Your Honor asked at the beginning of the hearing are my concerns as well. Other than that, we don't have any objection or reservation.

This tentative settlement from the trustee's side, Mr. Lobel's side, is great news to us. If it sticks, if it's good -- I don't know the details of it. But this is obviously something that has grown out of my lawsuit, my equitable subordination lawsuit. And I want to just be able to continue with it in Santa Ana before Judge Smith not in any way, shape or form intruding on the stay or the jurisdiction of this Court. And that's our position.

THE COURT: Let me just ask you one question.

MR. MILLER: Sure.

THE COURT: Who do you represent in that litigation?

MR. MILLER: I represent all of the debtors, the voluntary and involuntary debtors -- the trustee debtors and the voluntary debtors as special litigation counsel.

THE COURT: And as special litigation counsel, you

heard for the first time this morning that the trustee has worked out something that may result in a settlement of at least that party a lawsuit, is that correct?

MR. MILLER: No. I spoke to Mr. Lobel about it last Friday. And we've been discussing it. But I have not seen the term sheet yet and I don't know the nitty gritty of the details of it. So -- but he called me on Friday and we had a conversation about it.

THE COURT: I don't want to get into the specifics of it. It will either, as you say, stick or it won't. Presumably, it will stick. And at least that part of the litigation goes away.

MR. MILLER: I mean, what I heard sounded okay. I just need to see -- you know, the devil is in the details. And, you know, it's about half the case. It's the involuntary debtors, the trustee debtors. We still have to deal with the other half of the case. And we're working hard on it. And my lawsuit, quite frankly, is the driver of all of it.

THE COURT: Well, I know that's your perspective. I don't know if it's true or not. And I'm not approving your fee so it doesn't matter.

MR. MILLER: Thank you, Your Honor.

THE COURT: All right.

MR. MILLER: Appreciate it.

MR. PEREZ: If the opposition is withdrawn, I'll sit

down, Your Honor. Otherwise, I've got a couple of comments to make.

THE COURT: I think there's no one -- well, let me find out. Is there anyone else who has a comment about this pending motion? Apparently not. Mr. Perez?

MR. PEREZ: Yeah. Just a couple, three comments, Your Honor. Number one, one of our exhibits is a letter going back to January of this year where we informed the SunCal debtors that LBHI had an interest in these assets through the CP notes. I mean, there's no question about it. The record is clear. This is not anything new or different.

And furthermore, Your Honor, our motion clearly contained a full reservation of rights of the debtor so that we wouldn't affect the distribution among the various debtors' estates. And that's precisely what we're trying to do. Thank you, Your Honor.

THE COURT: Okay. Having heard the argument presented by the debtors, the support of the creditors' committee and the opposition by the SunCal voluntary debtors, which appears to the Court to have been more in the nature of a reservation of right as to the potential consequences in the SunCal bankruptcy case in California to approval of the unwinding of the structure, I am satisfied that sufficient business justification has been presented to approve the motion and that the undoing of the structure results in a number of claimed

benefits to the estate including the elimination of certain costs and the preservation of the rights of separate debtors so that the distribution rights of those creditors looking to particular members of the Lehman corporate family will unaffected by the approval of a settlement.

I'll entertain an appropriate order.

MR. PEREZ: Thank you, Your Honor. Should I tender the order now or --

THE COURT: At the end of the hearing.

MR. PEREZ: Okay. Thank you, Your Honor. Your Honor, the next matter on the docket is the motion to lift stay.

(Pause)

MR. O'KEEFE: Good morning again, Your Honor. Sean O'Keefe appearing on behalf of the SunCal debtors, the voluntary debtors. Your Honor, I'm a Chapter 11 reorganization lawyer and my objective is simply to reorganize the cases that I have been assigned to. In the current context in California, it's an inherently difficult process because this is a large land case and we are facing the largest property value of the clients since 1930. We also have a substantial secured creditor. The overlaying variable on that is that there is a litigation ongoing with that secured creditor. But our objective is not in any way to do anything other than to reorganize under Chapter 11 in our case. And I can't emphasize that enough.

Insofar as the characteriz --

THE COURT: Can I break in and ask a question?

MR. O'KEEFE: Yes, Your Honor.

THE COURT: Are you personally involved in the appeal of the BAP decision to the Ninth Circuit?

MR. O'KEEFE: Yes, I am. I'm the principal lawyer, Your Honor.

THE COURT: Are you the lawyer of record?

MR. O'KEEFE: Yes.

THE COURT: And what's the time horizon of briefing and adjudication in the Ninth Circuit?

MR. O'KEEFE: Your Honor, my recollection now is briefing is complete. But they don't tell you when they will set oral argument or if they're going to have oral argument. It's entirely possible that could take months or as much as nine months. So I just finished two appeals. And as a general rule, it takes a significant period of time. So I don't exactly know when they're going to set oral argument or whether they're going to rule simply on the papers. But they haven't provided us that.

THE COURT: Now, I take it that it's your position on behalf of the voluntary SunCal debtors that the BAP panel got it wrong when the BAP concluded that the SunCal debtors needed to come to this court to obtain stay relief in order to prosecute the equitable subordination litigation in the

bankruptcy court in California. Is that right?

MR. O'KEEFE: No, Your Honor. That -- there is no question in my mind that the home bankruptcy court determines the scope and application of the stay, as the BAP said, in the final resolution. So, for example, there was just a case, it's a published decision, where the Supreme Court in New York made a decision regarding whether or not the stay applied in that particular case. Every Court that confronts the stay has to make a determination does the stay apply on these facts.

THE COURT: Yeah. But I'm trying to understand whether or not in appealing the BAP decision, you're arguing that the BAP got it wrong when the BAP concluded that Judge Smith got it wrong when she concluded that you could properly prosecute equitable subordination litigation against the Lehman debtors without first obtaining stay relief here.

MR. O'KEEFE: Not the procedural issue but the substantive issue. Basically, our position is -- is consistent with what we read to be the law in this circuit. And in the Ninth Circuit, but for that one case, that the pursuit of an equitable subordination action whether through a contested matter or through an adversary proceeding is deemed defensive and consequently that does not violate the stay.

The second issue as to who gets the final say on whether the stay applies, we absolutely agree that the home bankruptcy court makes that decision. So now we have a

circumstance, we believe -- and we have absolute confidence that the BAP will be reversed. We think Judge Markell's decision states the law.

THE COURT: Are you saying you have absolute confidence that the BAP will be reversed?

MR. O'KEEFE: Yes, Your Honor. Yes, Your Honor. I just think that --

THE COURT: That's an unbelievable statement to make on the public record.

MR. O'KEEFE: Your Honor, the -- it is a decision which we think is directly contrary to the authorities of that circuit and we don't think that it will stand both jurisdictionally and substantively.

But we agree -- we agree, Your Honor, that if the determination of whether the stay applies in the final determination -- and that's what the BAP said. And the final determination is Your Honor. So we absolutely agree. So, for example, Lehman had the right to come back here and say there's this determination and we think it's in error. And had Your Honor said I think so, too, then that's it. We're stumped. There's no question there. We operated from that point going forward because Lehman raised the issue -- Lehman raised the issue with Judge Smith. Lehman filed the motion for relief from stay and said, Judge, we're making a motion under (d)(2) and (d)(3) that says this reorganization automatically fails

because our stay prevents them from subordinating our claims. Faced with that argument, Judge Smith said, well, that's not the law in this circuit. And also we have the Meddium (ph.) decision and Your Honor's decision in Shinsei. And maybe we are misreading that. But --

THE COURT: I think you are reading the Shinsei decision.

MR. O'KEEFE: And that's entirely possible, Your Honor. But I do believe that Judge Smith's decision based on their argument, and it was in response to their argument, she said I see, under (d)(2), an ability to reorganize pursuant to which they can seek to subordinate your claims. And on that basis, we proceeded. So they raised the issue and she ruled on it.

Now the BAP took that issue up -- and they didn't seek to set aside the order denying motion for relief from stay. They appealed just that narrow ruling, that issue of law, as to whether or not the stay was affected by an equitable subordination action, whether that was offensive or defensive. Prior to that point in time, we believe the law was clear that it was defensive. They view it, the BAP did, as offensive.

But --

THE COURT: That's consistent with Judge Gonzalez' decision in the Enron case as well.

MR. O'KEEFE: Your Honor, I think the correct

statement of the law is what was stated in the Meddium decision because I think what the Court is saying is, look, if you come to a case, we have to be able to determine the priority of your claim. And that's really what's going on here. Integral to our reorganization effort, we have to deal with the claims that they filed in our case. Conceptually, I think we can all agree that we could have objected to their claim, raised an unclean hands defense and a recoupment defense and, on the basis of those equitable affirmative defenses, sought subordination.

THE COURT: I understand --

MR. O'KEEFE: It's just that --

THE COURT: I understand your position on that. But one of the issues here is that through other counsel, in November of 2008, the SunCal debtors brought a motion for stay relief here which I denied without prejudice. It was very obvious, I think, to anybody who was present in court, including your partner, that one of the problems with the original motion was that overly broad, it didn't seek particularized relief. And from the very beginning of the SunCal bankruptcy, it was apparent that SunCal needed to deal with Lehman Brothers. I made it very clear that I would entertain other motions for stay relief or stipulations that the parties might enter into relating to stay relief.

But nothing happened. Except in January of 2009, I was involved in an emergency hearing, I believe it was on a

Friday afternoon, New York time, seeking to enforce the stay because, in effect, your debtors were treating this Court as if it had no say in the matter. Ultimately, I made some threatening noises on the record, and the record speaks for itself, that there might well be sanctions for a willful violation of the automatic stay. And until now, the SunCal debtors have absented themselves from this court. That's one of the reasons why I interjected earlier in your argument on the Fenway motion about your not having been here except when you needed to be here. I think you needed to be here a lot sooner. And I'd like an explanation as to why you haven't been here sooner.

MR. O'KEEFE: The first thing is, Your Honor, to the extent that we have engaged in any course of conduct that was offensive to this Court or that affected the stay, we sincerely apologize. That was not our point. To the contrary, I've been practicing bankruptcy law in twenty-five years -- for twenty-five years and nobody has ever accused me of violating the stay.

What happened in this circumstance was, Your Honor, we moved for -- the circumstance you're referencing -- and I'll just go back. Twenty years ago, I had a case, and it was only one in my whole career, where we had two cases, two debtors, who were looking at each other saying well, my stay applies and your stay applies. And we went to Mr. Klee (ph.) and Mr.

Tweester (ph.) because there were no cases anywhere on the issue that confronted that circumstance and said well, what happens, who has primacy. And their response was the Code doesn't work very well under those circumstances.

Well, since then, we've had more input from the case law. But the truth of the matter is, Your Honor, we've never run into this circumstance before. And insofar as that hearing you're referring to, we moved the use of cash collateral in that case and that was the issue that Your Honor is speaking to. And Your Honor told us I think that violates the stay and we withdrew that motion. The reason why we filed that motion is because there was another pending Lehman case, LB Rep, something or other, and it was represented by the same counsel. And the trustee in that case moved for the use of cash collateral and there was no stay assertion.

Now, going all the way back to the first motion for relief from stay, Your Honor is absolutely correct. And I wasn't involved in that. That motion was early in this case. And it basically was this blanket prayer for relief. I don't really understand why that motion was filed in that structure particularly given the fact that this was early in this case. It was going to be denied. It should have been more focused and Your Honor made that clear.

But insofar as that particular issue, the motion for use of cash collateral, Your Honor made your thoughts clear on

that and we withdrew the motion. And that was very difficult in a Chapter 11 to operate without the use of cash collateral particularly since the party who controlled the cash collateral or alleged that they controlled it was trying to crush our case. The next thing that happened in time, Your Honor, is they raised the issue before Judge Smith. They filed the motion for relief from stay saying our stay thwarts their case. You cannot succeed. You might as well give us relief from stay to foreclose on everything because they can't reorganize, period, because of our stay. That was the argument. It was a (d)(2) and a (d)(3) argument.

In response to that, we presented -- and in response to that, we presented our arguments and our case law saying that the stay didn't apply, that this was a defensive act and we could subordinate their claims. And the claims objection in priority determinations are traditionally to the extent they just affect the claim deemed defensive. And Judge Smith specifically ruled on that. It was only within the protection of that ruling that we proceeded. Now, Your Honor, they had the option to come to you and say, look, we think this is wrong. And whatever Your Honor said, that's the law. That's it. We agree. There's no dispute. But they didn't do that. In fact, thereafter, they affirmatively represented to Judge Smith over and over again the stay doesn't apply. In fact, I will tell you that I went to court once to complain that the

motion -- the agreement we entered into -- because when Your Honor said we couldn't move for the use of cash collateral, we had to enter into a very onerous financing agreement. And what was discovered after the fact is that they didn't hold the lien or even the claim. And so, when we went in again, I said you know, there's something unfair about this. They invoked the stay with respect to a loan and a lien they don't hold and now I'm stuck with this onerous financing agreement which they should never have had in the first place because that's not their lien.

At that point, Mr. Pachulski, an exceptional lawyer, jumps up and scolds me in front of Judge Smith and says that stay has not been an issue in this case for months. And that's in their disclosure statement.

So maybe it was incorrect for us to rely on Judge Smith's ruling. But they invoked that issue. And she responded and ruled. And we, in reliance on that, went forward. And they could have come to Your Honor and said Your Honor has the final say and we agree. There's no dispute. But they didn't do that. They said the stay does not apply over and over again. And it's in their own pleadings.

So to the extent that we have proceeded in a manner that's procedurally inappropriate, we apologize. That was not our intent. We thought we were doing the right thing. And I have to tell you, Your Honor, I'm a debtor moving for relief

from stay. That just seems -- I mean, it's just a new thing for me and for everybody out there. There just isn't a lot of case law on this.

THE COURT: Mr. O'Keefe, I understand your position. But here's the concern that I have and it's actually the flipside of the argument that you were making in the context of the unwinding of the Fenway Capital commercial paper program. And that's the question of good faith. I couldn't have been clearer in January of 2009 that this was the Court that you needed to come to for purposes of getting stay relief, in that instance, relating to the use of cash collateral.

But it's now May of 2010. It's quite a long while after that. And one of the concerns I have is that Judge Smith and I are players in a cross-country game of gaming the system, of using courts to your particular purpose in order to gain strategic advantage. And speaking for myself, I don't like that. I suspect that Judge Smith would say the same thing if she were here.

MR. O'KEEFE: Your Honor, all I can do is apologize. The reality is there was a ruling; we did rely on that. They did have their procedural remedies. Maybe in retrospect that was not the right thing to do but rather to take that and immediately come back here. And in retrospect, given Your Honor's insight, that's what I would do.

THE COURT: Let me ask you a question. Assuming that

you are successful in the Ninth Circuit whenever that happens, what's the consequence of that successful prosecution of the appeal of the BAP decision to the Ninth Circuit? What happens then? Does it moot my need to decide the pending motion?

MR. O'KEEFE: Your Honor, I don't think it does. And this is just my analysis of the law. Essentially, the BAP was correct in one respect, that, procedurally, to the extent that there is a final determination who trumps everybody insofar as the determination relative to the scope and application of the stay, it is the home bankruptcy court. So if you make a determination with respect to that issue, then our only recourse is to appeal. That's it. That's the only option we have.

The mechanical -- the effect of the BAP being overruled is there is a case in the Ninth Circuit which determines that a particular course of action in isolation -- and again, they didn't appeal the merits of the order denying the motion for relief from stay. And subsequently, we brought to them they didn't even own these loans so the motion shouldn't have been brought in the first place. So that's our jurisdictional issue. But if -- and we believe the Ninth Circuit will reverse this, even if just on jurisdictional grounds to say why are you here. The motion shouldn't have been brought, the appeal wasn't valid. It's all vacated.

But what we think will happen is we'll clarify the law

in our circuit. And that's really, at this point, what we're trying to do. Insofar as your determination, the reality issue, Your Honor, we have no dispute that to the extent the stay applies, the home bankruptcy court gets to say it applies. And you trump everybody else. And at that point it's solely --

THE COURT: I'm asking you a slightly different question. And you may have answered it and I just didn't fully understand the answer. If you are successful in the Ninth Circuit, would you be able to prosecute the litigation against the Lehman debtors for equitable subordination in the bankruptcy court in Santa Ana without obtaining stay relief here? That's a yes or no question.

MR. O'KEEFE: Under Baldwin-United, yes, Your Honor --

THE COURT: In that case --

MR. O'KEEFE: -- unless --

THE COURT: -- then the Ninth Circuit adjudication could moot the pending motion here, correct?

MR. O'KEEFE: If Your Honor --

THE COURT: That's a yes or no question.

MR. O'KEEFE: It would depend upon the ruling, Your Honor.

THE COURT: That's a yes, no or I don't know.

MR. O'KEEFE: I would say yes, if it's before the ruling. Yes, because if they decide that the BAP is overruled, then at this point, Judge Smith's ruling with concurrent

jurisdiction, but not final -- Your Honor gets the trumper, we agree with that -- every Court has the right to determine whether the stay applies. So if she determines the stay doesn't apply and nobody comes back here then that's the law of our case and we proceed on that basis.

The -- so it would be a timing issue. Now, on the other hand, if Your Honor were to determine the stay doesn't apply, okay, then the Ninth Circuit would potentially -- someone could argue it's an Amwell (ph.), maybe that moots that issue because the home bankruptcy court has ruled it doesn't apply. We were not -- we want that decision vacated for a lot of reasons.

But I think that would be the result. So I think it's a timing issue. And I don't mean to be evasive, Your Honor, but -- I mean, the bottom line is we do need a resolution and we're looking to Your Honor to give us that.

I would note that subordination -- basically, dealing with these claims, a lien priority dispute, is integral to the plan of reorganization. It's going to be very difficult for us to reorganize without resolving the claims against the estate. At this point, Your Honor, all the folks, the defendants, are all nondebtors, all nondebtors. This motion -- this transaction is bringing them, they believe, back into that case. Now, what Judge Smith did was say, okay. I agree. The BAP controls; LCPI has to leave. So she dismissed them;

they're gone. There are no debtors in the litigation. The issue is do they get, through this transaction, to just come right around and buy a claim, in effect, go right back to Judge Smith and say I'm sorry, we're here again. We still get to thwart the litigation which has a material adverse effect on my ability to confirm a Chapter 11 plan. And that's really in our mind what's going on here because they're all nondebtors.

Now, the whole argument, Your Honor, that we're the aggressor in this -- Your Honor, there's only ten lawyers at Winthrop Couchot. And only two and a half, on a good day, can work on this case. These folks have hundreds of them. These are the two largest bankruptcy firms in the United States. I'm working seven days a week, get up at 6:00 on a Saturday morning and they have unlimited resources. So if the concept is that I'm kicking them around like a can, that's not happening. It is absolutely to the vice versa.

THE COURT: You can put this on your website, it's good for marketing.

MR. O'KEEFE: Your Honor, the merits of the claim that LBHI stay will apply premised upon the contention that they're going to attach a lien to the loans. And I've already gone through that. They stated in their motion, the MRA is gone, and that's the basis for the lien. They state that the guarantee is terminated. They state that the CP notes are terminated. So this is some sort of leap-springing lien that I

don't understand. And it's a lender of a lender. That is too indirect for the stay to apply.

And, also, to the extent that that's their design. You shouldn't be able to buy into a piece of litigation that's going on in a bankruptcy court and ten stand up and say you know what, I knew it was happening, but I'm here and you're stayed. That's just something wrong with that.

Your Honor, we've had a back and forth relative to whether or not a subordination action is subject to the automatic stay. We can all agree that a claim objection is not subject to automatic stay. And a claim objection can effectuate the complete disallowance of a claim. If the claim is disallowed the lien goes away.

What we're trying to do is to subordinate to the extent necessary to deal with the creditors who they've created by authorizing work. We don't think that is subject to the stay. Your Honor may have a different opinion. But if that's the case, I would simply say to Your Honor that it's very difficult to do a reorganization if you can't deal with claims and liens against your estate.

So conceptually both cases should be able to proceed. And Your Honor should be able to fashion, and I note that the creditors' committee, although they object to this, say as a secondary position that Your Honor could have a reporting system or other controls that would assure that your case was

not affected. But it can be that a grader or a framer in California doesn't get paid and the creditors in this case gets paid. There has to be a medium where they both can proceed.

The problem that we have from a balance of the harms perspective, and basically our orientation under Sonnax was, these huge properties are sitting there. Every weekend I drive passed one. And it is this giant expanse of land with dust blowing around in the midst of a city. And there are fire issues, there are flood issues, there are dust issues. We can't solve that problem until we deal with this claim. So delay has a material affect on our asset and theirs. Nobody gains by delay. This is not a solution, it is simply a -- in our estimation an issue of litigation leverage. The pricing of a future settlement, and that's not a basis -- that is not a harm for them. But it is a severe harm for us. I don't know that we don’t have relief from stay.

THE COURT: All right. Let me just see if we can accelerate through the rest of your argument. Because we've been going at this for a long time, and we have a very full courtroom still.

MR. O'KEEFE: I apologize, Your Honor.

THE COURT: No, you have nothing to apologize for. But as you point out you're not exactly a party-in-interest here.

MR. O'KEEFE: Well --

THE COURT: You're a party-in-interest, representing the interest of the SunCal debtors and I appreciate that. But I think we need to move it along.

MR. O'KEEFE: Then I would simply submit to the Court as we've gone through in our briefs, that to the extent the stay applies, to the extent that Your Honor determines that it does apply, Your Honor should lift the stay to the extent necessary to allow the action to proceed.

One of the points that Mr. Miller made was there is a settlement. Your Honor, this case will settle. I can't guarantee that for sure. But the reality is there is a dynamic here, the parties where they initially weren't talking, now they are talking. The truth of the matter is, the stay will just cause delay, it will shift litigation leverage and it isn't a solution.

So we have addressed the Sonnax factors, we are asking for limited relief from stay. To the extent that we've offended the Court I sincerely apologize, that was certainly not our intent. We thought we were doing the right thing.

THE COURT: Okay.

MR. O'KEEFE: Thank you, Your Honor.

THE COURT: Apparently Mr. Miller is going to be brief.

MR. MILLER: Be very brief. Learning more about bankruptcy law and bankruptcy stays than I ever knew before.

Your Honor, I just want to very briefly, because I think it's been well addressed. I just want to answer Your Honor's question about, you know, why didn't you come back sooner? And this is from my perspective as a trial lawyer, a litigation lawyer, not a bankruptcy lawyer.

In March of '09, Judge Smith -- I was there, they moved for relief from stay so they could foreclose. And Judge Smith in her order, I'm quoting, says "that her court has concurrent jurisdiction to determine the scope or applicability of the automatic stay under 11 U.S.C. 362(a)." And she said "the automatic stay arising from the bankruptcy case of Lehman Commercial Paper does not apply to any proceeding to subordinate the claim of Lehman Commercial Paper and/or to the transfer of the lien," so forth and so on.

So, you know, we won, we thought we were golden, and to the extent we should have come back here -- this is my take on it, we should have come back here with this order since I gather from my lesson this morning this Court has the final say on the debtor before this Court's stay. We probably should have come back here with this order. And to the extent we didn't, we're sorry.

The BAP then reversed at the end of the year. And when the BAP reversed we had this ruling from Judge Smith that LCPI had sold the loans to Fenway, all of them. So it didn't seem like LCPI was part of the case anymore, or that the stay

was implicated.

Then we get this compromise motion, and we say whoa, this compromise motion brings LCPI and Lehman entities back into the picture, we better fire up our motion for relief from stay. So here we are, okay. Here we are. And to the extent we should have done it sooner, we should have done it sooner. But there was no intent, at least from my perspective, to ever avoid or evade the jurisdiction of Your Honor, and, Your Honor, the stay in this court. Okay, so that's number one.

Number two, very briefly. My ultimate -- I'm representing the debtors, but my ultimate clients are, like Mr. O'Keefe said; the grading contractor, the drywall, the guy that does the sidewalks, the retaining walls, they're all in California, all the documents are in California. We filed our lawsuit in January of '09. We've virtually completed document discovery. Mr. Lobel's been working real hard, and I'm hoping this settlement sticks for part of the estates, frankly. I'm hoping it seeps over to the other estates, if we can work that through. I'm working with him and with his office, and it's going to take a lot more work, but I don't want to change the playing field. And that's why we're here, Your Honor. We want to be able to maintain the playing field as it is right now. I've got my lawsuit, we're litigating equitable subordination. I'm beginning to think they think we have a pretty good case based on what I'm hearing on this settlement that Mr. Lobel's

been negotiating, but, you know, I'll put that on my website or something.

THE COURT: No, I suggest you don't do that.

MR. MILLER: I just want to be able to keep it going and not have to go back to California and say well, we're going to try the case there against the nondebtors, because there's no stay implicated. But then we've got to take some of the same creditors and come back to Your Honor, and basically retry the same case and do it twice. And that's exactly -- I was reading the papers on the plane, in a footnote that's exactly what they say they -- that's exactly what they suggest. They suggest that they could have requested that the entire equitable subordination be tried before this Court, but they're not. They just want the LCPI piece here and I guess the nondebtor piece in California. That doesn't make any sense. That is -- I think that's gaming the system. That's just a litigation tactic, it's clever, very smart lawyers. But it's just repetitious, duplicative.

I'm sure this Court is, you know, very, very busy. I know Judge Smith is very busy, because I've spent half of my life there over the last year. And I would just request Your Honor to enter relief to the extent it's necessary so that we can do it all in California.

THE COURT: All right.

MR. MILLER: Thank you, Your Honor.

MR. PEREZ: Your Honor, Alfredo Perez. A couple of comments.

I hear counsel saying that they believe that the home court has the last say on the automatic stay. Unfortunately, I believe that their actions really don't support that.

And, in fact, Your Honor, if the Court looks at the equitable subordination claim, one of the predicate acts, if you will, to the liability for equitable subordination is -- are improper attempt to enforce the automatic stay before this Court. So it's completely -- this pleading completely belies the mea culpas that we've heard this morning.

Second, Your Honor, as it relates to whether the stay apply, I don't believe that there's any question but that the stay does apply. The BAP found that the stay applies, in connection with their equitable subordination claim. I mean, what they really want to do, is they really want to strip our lien. It's not the situation that you had before Judge Drain, where you're reordering priorities. And I read Shinsei three times and the Court basically says under these circumstances involving Japanese law, it's limited to these facts. I don't think that's a broad ruling that equitable subordination is defensive in every ruling. Judge Gonzalez's ruling in Enron says it's affirmative. So I don't believe that there's any question about the fact that the stay does apply.

Now, let me address what I believe is the key Sonnax

factors, and that is balancing of the harm. Your Honor, at this point -- and we could have, by the way, I'll take up Mr. Miller's point. I mean, we could have requested that the whole thing be moved here. And as a practical matter, we didn't think that was appropriate because, first of all, in view of this Court's docket and the fact that it's basically their claim. So we didn't think that was appropriate.

But we also don't think it's appropriate for the stay to be lifted at this time. There may be an appropriate time for the stay to be lifted. But there are probably three or four -- what I think are very compelling reasons why the stay shouldn't be lifted.

The first one is, Your Honor, we need to see the settlement through. We need to see what ends up at the end of the day. Now, there are -- there has been LCPI loans that weren't in Fenway, that have always been the subject of the stay regardless of the Fenway deal. So we really need to see that settlement through.

We also need to see what the BAP does. I mean -- and I think the Court's --

THE COURT: I think you mean what the Ninth Circuit does.

MR. PEREZ: What the Ninth Circuit does, I think you're -- and I think Your Honor's play was absolutely upright. And, frankly, if I was in Mr. O'Keefe's shoes I probably would

have done the same top dance in response to your question. Because I think the answer based on their papers is yes. It would moot it. I mean, that's basically what they were telling you. Yes, if you read their papers, that's what they said. That's number one.

Number three, Your Honor, I mean we are regardless of whatever anybody says, at a critical time in this case. I mean, filed a plan, we filed a disclosure statement, going to file the motion to approve the disclosure statement hopefully this Friday. That's one of the things I'm going to do when I get back. And we're going to prosecute the plan. And it's going to take a while, but we're affirmatively going to prosecute the plan.

And to the extent that we are able to resolve the thing with seventy-five percent of the value, I think that's -- that's going to instruct a lot better as to how the balance gets resolved. And continuing to litigate in my mind doesn't -- I mean, it's great for Mr. Miller to come up here and take credit, you know, for something that he learned about on Friday, that's terrific. But the fact of the matter is is that despite those efforts, I mean we are trying to reach resolution. We're trying to reach a resolution with all our constituencies, that's not something that we take lightly.

I mean, if our goal was to litigate, Your Honor, as the Court well knows, you know we could be here 24/7, you know,

until we're both very old. And that's not our goal. I mean, our goal is to try to resolve these matters as expeditiously as possible. And I think we are making progress.

So, Your Honor, at a very minimum I would request that the Court defer the stay. I think the Court should deny at this time, without prejudice, and let them resurge their motion.

And, by the way, Your Honor, the thought that they can't craft a plan that they do come back here and say this is our plan, we'll set up a litigation trust, we'll do whatever. I mean, that's what people -- that's what people normally do. And come to Your Honor and say you know, we'll -- we want the stay lifted so we can prosecute this plan, this sets up the litigation trust. I don't see any reason why something -- and basically the Court had invited them to do that. And they haven't done it.

So for all those reasons, Your Honor, we think the motion should be denied.

THE COURT: Is there anything more?

MR. O'KEEFE: Your Honor, just one minute. Counsel's comparative with a balance of harms is that they need apparently an allocation of resources relative to filing their plan. Certainly, they have more than sufficient resources between the firms that they have working on this, and they also have a professional firm managing the debtors' liquidation.

In contrast, the balance of the harms, the delay on our part, is the properties, Your Honor. These are huge pieces of property that probably stretch from here to the Hudson. So -- I mean, some of these are ten thousand acres. They're in the midst of cities, there are material issues that we have addressed. So there is a fundamental difference, the balance of the harms tip sharply in our favor.

Insofar as the concept of settlement should delay the litigation, certainly Your Honor has participated in this process on both sides of this to see that litigation, if there is a stay, the settlement might go away, or alternatively it will change. Certainly, the litigation is a driver for settlement and it will expedite that process to our mutual benefit. Thank you, Your Honor.

THE COURT: All right. This took quite a bit longer than I anticipated. And it's a complicated question. One of the things that I believe complicates it is the fact that there is an appeal currently pending before the Ninth Circuit court of appeals from the decision of the Ninth Circuit Bankruptcy Appellate Panel. And I believe, but don't know, that it is more likely than not that successful prosecution of the appeal in the Ninth Circuit by the SunCal debtors in fact will moot the motion which is before me.

There's a corollary, however, which is my granting the pending motion may to some extent moot the appeal. This is

another example of what we've been colloquially calling gaming the system, in effect, using litigation to gain tactical advantages. In this instance, litigation which has gone all the way to the Court of Appeals level in the Ninth Circuit and litigation which was not brought here for stay relief that could have been brought earlier.

Ultimately, the question of whether or not I should grant relief from the automatic stay is driven by my application of the Sonnax factors. And both parties appear to be focused most heavily on the balance of harms factor. That's convenient because I prefer to focus on that one myself.

One of the reasons I have a difficult time finding that there is any material harm to the SunCal debtors in not granting their motion for stay relief is that they did not bring it until now. The SunCal debtors have scrupulously avoided coming into this court from November of 2008 until today. And have managed to deal with their litigation requests in the bankruptcy court and beyond apparently without material impairment in those efforts. In effect, they've elected their remedy. They have chosen to proceed with litigation in their home court. And when they suffered a reversal at the BAP level at the end of last year then had to review their strategy again.

Having gone to the Ninth Circuit, I believe the Ninth circuit is the place for this question to be decided. And I'm

going to defer my decision with respect to stay relief until after the Ninth Circuit has acted.

Moreover, and I think this is a very significant point, the existence of the stay is not inconsistent with the pursuit of negotiations that could lead to a resolution of this ongoing dispute. The fact that the involuntary debtors, through their trustee, appeared to have reached an agreement in principle resolving many, if not all, of the same issues that are set forth in the equitable subordination complaint, demonstrates that it's possible for the parties to engage in potentially productive discussions, notwithstanding the fact that they stay remains in effect.

To the extent that the existence of the stay is viewed as an impediment of any sort to meaningful dialogue, I want to be absolutely clear in saying that I do not believe the stay impacts in any adverse way the ability of the parties to meet and confer -- to mediate or to otherwise seek a constructive resolution of the matters that are currently before the bankruptcy court in the Central District of California.

As to active litigation, the motion is denied without prejudice to being reconsidered at some later time in the case, either before or after the Ninth Circuit has acted.

And I will consider an appropriate order consistent with what I've just said.

MR. PEREZ: Your Honor, we'll prepare one and submit

it to counsel.

THE COURT: Fine.

MR. O'KEEFE: Your Honor, can I ask a few clarifying questions?

THE COURT: You can ask.

MR. O'KEEFE: Is the Court --

THE COURT: The motion's denied. I want to be really clear on that. Your motion is denied.

MR. O'KEEFE: And I'm not rearguing the motion, Your Honor.

THE COURT: Fine.

MR. O'KEEFE: So the Court -- is the Court finding the stay applies and the motion is denied?

THE COURT: The stay applies and the motion is denied.

MR. O'KEEFE: Is the Court finding that insofar as LBHI -- what is the Court's finding with respect to the application of their stay?

THE COURT: I'm not making any particularized findings. And let me be really clear, the law in the Southern District of New York as stated by Judge Gonzalez in the Enron case, and I choose to follow his reasoning, is that litigation brought by a party against a debtor seeking to equitably subordinate claims of that debtor constitutes a violation of the automatic stay. To the extent that there are debtors or debtor property implicated by your litigation I am saying the

stay applies. And I'm not going to say more than that. And I think it's a good time for you to sit down.

MR. O'KEEFE: Very well, Your Honor. We appreciate the Court's time and consideration.

THE COURT: Sure.

MR. MILLER: I just wanted to thank the Court for the pro hac vice admission, and for hearing me this morning. Thank you.

THE COURT: No problem at all. And then just so it's clear what my view is of the Shinsei case because that has been liberally misquoted in papers, my ruling with respect to the Shinsei case speaks for itself. But I view actions taken pursuant to principles of Japanese bankruptcy law which would have the effect of subordinating claims, not to be covered by the principal announced by Judge Gonzalez in the Enron case because under Japanese law active litigation comparable to an adversary proceeding is not involved. And in that case the action taken by Shinsei Bank was not self executing and involved actions to be taken by a quasi judicial figure, a supervisor, who would be determining whether and when a competing plan would be circulated to creditors. It was incredibly fact specific, and is not subject to broad application in the U.S.

MR. PEREZ: Thank you, Your Honor. May I be excused, Your Honor?

THE COURT: Yes.

MR. PEREZ: I believe, Your Honor, the balance of the matters on the docket are not being handled by our firm, Your Honor.

(Pause)

MR. TAMBE: Good morning, Your Honor.

THE COURT: Good morning.

MR. TAMBE: Jay Tambe from Jones Day, counsel for the debtors.

I'm addressing items 4 and 5 on this morning's agenda.

Number 4 is the motion of the debtors for an entry of order to consolidate certain proceedings. And the proceedings we are seeking to consolidate are basically three. There are two adversary complaints, one each against Nomura International and Nomura Securities. And also we are seeking to consolidate an objection with respect to Nomura GFP.

We've had some developments, I think we've resolved part of the motion, and we're seeking to adjourn part of the motion. I can address those issues if the Court would like.

THE COURT: I'd be delighted to hear about the resolution.

MR. TAMBE: With respect to International and Securities, those two entities did put in a response to the motion to consolidate. And those two entities have expressed concerns about consolidation off an evidentiary hearing or

trial. They have not expressed concerns, and I believe are in agreement with us, that for pretrial purposes; discovery, fact discovery, expert discovery, and in our view, dispositive motions, those two adversary complaints, one each against International and Nomura Securities should be consolidated for pretrial purposes. And we are prepared to hand up this afternoon, after we've discussed with counsel, a proposed order that would set out that agreement and the consolidation for pretrial purposes.

With respect to Nomura GFP we have had some discussions with Nomura GFP. We have granted them a brief extension of time to respond to the motion to consolidate. And with respect to whether or not GFP should also be consolidated for pretrial purposes, we've adjourned that part of the motion until the next omnibus hearing.

THE COURT: Okay. Does that resolve -- Mr. Bartner, do you wish to speak?

MR. BARTNER: Your Honor, Douglas Bartner from Sherman & Sterling for Nomura International, Nomura Securities, and Nomura GFP.

Just to confirm what Mr. Tambe had said, that's accurate.

THE COURT: Okay.

MR. BARTNER: Thank you.

THE COURT: Does that resolve item 4?

MR. TAMBE: That resolves item number 4, Your Honor.

THE COURT: Okay.

MR. BARTNER: May I be excused, Your Honor?

THE COURT: You may be excused.

MR. BARNTER: Thank you.

THE COURT: Item 5 is the motion to compel performance by Norton Gold Fields Limited.

MR. TAMBE: Good morning, Your Honor, Jay Tambe from Jones Day for the debtors, on item number 5 on the agenda.

This, the debtors' motion, the motion of LBCC and LBHI, to compel performance by Norton Gold Fields Limited of its obligations under an executory swap contract, and to enforce the automatic stay.

There are several arguments that are made by Norton, some are unique to this situation, others are common to matters that the Court has resolved on other swap contracts that have come before the Court. We are prepared to proceed, unless the court has specific questions. I will address the issues that are unique to this arrangement.

THE COURT: I'm going to give you a chance to do that in a moment. I just have a number of procedural questions, which, frankly, could be answered by both you and counsel for Norton Gold Fields.

One is why did it take so long for this matter to come to the agenda. The motion was originally filed in November for

a hearing in December of 2009. It's been almost a six-month delay, highly unusual. So one question is what's the reason for the delay?

Two, is certain of the papers filed by Norton Gold Fields make a passing reference to alternative dispute resolution procedures being requested. I'm not sure by whom, I'm not sure if the request was rebutted. I don't know why this isn't going to ADR.

So question one is why so long? Question two, why not ADR?

MR. TAMBE: The answer to both question is the following: There have been principle to principle meetings, several of them. And which began, in fact, before the motion was filed, continued in fits and starts over the course of the last six months. And there were times when it appeared there might, in fact, be a consensual resolution in the making that was a change in management. I don't want to go into the details --

THE COURT: I don't want the details.

MR. TAMBE: -- but it was discussed. But the parties were in discussion. And that's, in fact, why the motion was adjourned from time-to-time.

I can address their reference to ADR. This is a case where there certainly has been no shortage of an open communication corridor for principals to discuss a potential

consensual resolution. That has not been achieved and that's why we're going forward today, Your Honor.

THE COURT: Okay. Before getting into your affirmative case, I just want to give counsel for Norton Fields an opportunity to just deal with the question of ADR, and whether ADR has been formally requested. And if not, why not?

MR. TILLINGHAST: Your Honor, Edward Tillinghast from Sheppard Mullin on behalf of Norton Gold Fields.

First, just to briefly address the Court's first question about delay. Counsel for the debtor is correct, there have been negotiations that are going on going back to November of 2008. And a number of meetings in person and otherwise, that have not let to settlement at this point. Although, we thought we were close at different points.

With respect to ADR, obviously there was the application to utilize ADR that was approved by Your Honor sometime ago. We were, frankly, expecting to go to ADR and be part of that process. And then they served the motion and wanted to proceed with a motion. So we have no objection to going to ADR.

THE COURT: Okay. I'd like to know, and it's great that Mr. Gruenberger's here, because you're so proud of the consequences of the ADR program. Jones Day is handling this so this isn't a question for Mr. Gruenberger, it's a question for Mr. Tambe.

Why isn't this going to ADR? I looked at papers in this case that the initial Norton Gold response was sixty-seven pages long. It's one of the longest pleadings I've seen in a contested matter. And that's not a compliment. I mean, the papers were well done, but they appeared designed to obfuscate and overly complicate and create leverage through density. Why isn't this going to ADR?

MR. TAMBE: I think two responses, Your Honor. There was some reference made in the Norton papers, that there was some request or conversation that was had requesting ADR as initiated by their side, and the request may have been to Weil. We have conferred with folks at Weil, we don't believe any such request was made.

But, secondarily, there have been active hands on face-to-face meetings preceding to the last six months.

THE COURT: But if it's, in fact, true what Mr. Tillinghast says, and I have no reason to doubt it, that at various times the parties have been close to a resolution, isn't this just an enormous waste of your time and mine to be litigating this issue now? Because I'm inclined to suggest that is this isn't resolved by ADR based upon my review of the papers, there's a need for evidentiary hearing. There was a request in the initial response for an evidentiary hearing, some argument about whether or not this should or should not be by means of adversary proceeding, which I view as more of a

request for an evidentiary hearing, than a request that you change the form of your relief. But there are lots of fact questions that appear to be in dispute.

So one of the things I'd like you to focus on in your argument, in addition to why we're here, is whether or not we, in fact, do need an evidentiary hearing. And if not, why not?

MR. TAMBE: Let me start with the ADR process. I mean, certainly we have looked very carefully now for proposals and counterproposals, and we agree with Your Honor, we agree with the enormous effort that has gone into setting up the ADR process, and how successful the ADR process has been.

And, yes, there was a point in time when the parties were making progress. That is no longer the case. In fact, without again going into details, I would suggest that things have moved in the wrong direction in the last set of negotiations. I won't characterize it beyond that.

In terms of the evidentiary hearing, I will address that. I will address that as I go through the argument with respect to what they claim are factual issues that implicate potential factual disputes that would require to be resolved by evidentiary hearing. And I think with respect to each of those supposed factual issues, the very documents they've put before Your Honor, the very legal issues that spring from those documents, and the arguments they want to draw based on those documents and e-mails, they're all dead-ends. I mean, you

could resolve those factual issues right now in their favor, and they would still not be entitled to avoid performance under the contract. So while they may want an evidentiary hearing, while there may be all sorts of interesting facts that they want to discover, as a practical matter for what's relevant to resolve the relief requested by the debtors, those are all immaterial facts. As a matter of law they fail.

THE COURT: Why don't you proceed with your argument recognizing that one consequence after we're all done is that I may persuade both sides to spend time between the conclusion of any argument and any ruling in an ADR proceeding. Which raises a question as to whether you want to go through the process of arguing it, or whether you want to meet and confer about the desirability of ADR. It may or may not be helpful to the process to have a record which includes interaction with me as to how I view various arguments; like repudiation and promissory estoppel. And whether or not this is or is not like Metavante.

MR. TAMBE: I'm detecting a strong hint, Your Honor, but maybe I should confer with my client briefly about the suggestions made by Your Honor.

THE COURT: I think it would be a good idea for us to take a five-minute break since this is the last item on the morning calendar. And for you to confer with your client, and also to confer with your adversary to see if ADR may not be the

way to go before getting into the merits.

MR. TAMBE: We appreciate that, Your Honor.

THE COURT: Because I've read the paper, I have some views, but it may be better to the ADR process for me to keep my views to myself for a while.

MR. TAMBE: We'll certainly have those conversations. Thank you, Your Honor.

THE COURT: Okay. Let's take a five-minute break.

(Recess from 12:00 p.m. until 12:12 p.m.)

THE COURT: Be seated, please.

MR. TAMBE: Your Honor, we had a chance to consult with the client, and with opposing counsel. What we would propose is the following -- what we've agreed to is the following:

Which is to adjourn the motion for sixty days. The parties will jointly submit the matter for mediation before a neutral -- we won't strictly follow the mediation procedures, because the issues have been briefed to such great extent. I think we can use those briefs as our mediation submissions.

THE COURT: Right.

MR. TAMBE: And try to, in an expedited way, get a neutral involved in maybe facilitating discussions between the parties.

We'd like to have the motion adjourned for sixty days. In the event we're not successful, we will be back before Your

Honor. But we are hoping that we do get the consensual resolution.

THE COURT: I think that's a very good and workable approach, and I encourage both parties to work in good faith toward a resolution. And if you can't at least I don't have to read the papers again, I just have to remind myself as to what they say. So that's fine.

MR. TAMBE: Thank you, Your Honor.

MR. TILLINGHAST: Yes, that's acceptable. And thank you for your time.

THE COURT: Okay. Is there anything more -- I think this morning has been concluded --

MR. TAMBE: I think that was the last item on the agenda for this morning.

THE COURT: Fine. We're adjourned then until the 2 o'clock calendar to deal with adversary proceedings.

(Recess from 12:13 p.m. until 2:02 p.m.)

THE COURT: Please be seated.

MR. MILLER: Good morning, Your Honor -- good afternoon.

THE COURT: Good afternoon.

MR. MILLER: Good afternoon, Your Honor. I'm Ralph Miller here from Weil Gotshal & Manges on behalf of debtor, Lehman Brothers Special Financing Inc., known as LBSF, on the first item on the afternoon agenda, number 6, which is a status

conference in adversary proceeding number 09-01242.

I believe there are two matters of housekeeping that we'd like to deal with to report to the Court, and there is one issue that we may need to discuss with the Court, which has been to schedule our motion that's been filed, BNY Corporate Trustee Services.

First, as a matter of continuing to keep the Court informed of developments in the United Kingdom, we have received notice that the Supreme Court of the United Kingdom has tentatively set argument on the appeal in the Perpetual and Belmont cases, which the Court's familiar with, for the time period from March the 1st through March the 3rd of 2011. We understand this may change, but it is likely to go later if it moves at all. It is only a tentative argument setting.

Second, we have noted that we're not certain that all the letters between the courts are in the docket. And we've conferred with Mr. Mastro and Mr. Schaffer and I think we're all in agreement that if there are any of those letters that have not been entered on the docket, they should be entered on the docket. We'd request the Court's permission to check the docket if any of the letters are missing, to go ahead and put them in the docket, so they're in the record.

THE COURT: That's fine. Absolutely.

MR. MILLER: The third matter, Your Honor, has to do with the motion for entry of an order, alternatively to open

and reargue the parties' cross-motions for summary judgment. It has been filed by BNY Corporate Trustee Services. There's been a good bit of conferring about this. And I think we have reached agreement that if this is going to be heard under the case management order regular schedule that it is eligible for setting -- all parties agree its eligible for setting for the June 16th omnibus hearing date. However, we recognize, Your Honor, on behalf of LBSF that the Court declined to set a briefing schedule the last time we were together, and we certainly do not presume to want to set a briefing schedule if the Court does not wish to do so.

We would point out to the Court that this is a case in which LBSF is the plaintiff and is seeking money. And LBSF is in no hurry to try to move this forward faster than the coordination between the courts would require. And we believe that, in fact, there has been a exchange of correspondence which supports the fact that this Court has given assurances, and in which the Court has given requests that there be an effort to coordinate these matters. We would point out to the Court that BNY does not have any of its own money involved, it is the trustee and the parties who do have their money involved, have not come to the Court and asked for any expedition.

So we don't really understand that there's any party withstanding who is in a hurry to try to rush the process or

basically deviate from the understanding between the courts.

We also point out, as I think the Court knows, that there are many ways that the developments in the U.K. could make this moot. It's a classic interlocutory situation in which there may be no need for appellate time, for example, to be spent, because if the English court agrees with essentially the outcome of this ruling, although it's under the anti-deprivation principle as the Court know, which is not exactly the same doctrine, but if it reaches the same direction of its result then that may make this decision moot. If it does not then it's certainly possible that that my open some other opportunities for resolution. And it's also possible Perpetual might choose to appear in this case at some point, depending upon what happens there.

So for various reasons LBSF does not believe there's any need to enter an order and there certainly is no urgency, we believe, in reopening the parties' cross-motions for summary judgment. So we would suggest that this motion is not one that needs to be heard on any sort of an expedited basis.

We have talked with Mr. Mastro, he's going to ask, I believe, for an expedited briefing and hearing schedule. And we've given him the earliest date that LBSF believes it could prepare a response, that we would point out that is going to get relatively limited time for a reply, and relatively limited time for a review of the completed papers before the courts

would have to hear the matter. And, also, we would note a couple of scheduling items. And then I'll let Mr. Mastro talk about his motion.

First of all, we all note that the Memorial Day holiday is in the middle of this scheduling period, it's Monday, May the 31st. And as a matter of just personal disclosure to the Court I have either a large mediation in this matter, and then I have a trustee motion set for two days in bankruptcy court in Delaware that occupies the period between June the 8th and June the 15th. So that particular time I happen to be personally conflicted.

However, there are ways to set up a briefing schedule, we believe as early as June the 7th, which is a Monday or -- or June the 4th, if the Courts wanted expedited briefing. But, again, that's not what LBSF is asking for, we're just trying to cooperate.

So with that, Your Honor, I believe Mr. Mastro wants to discuss his motion with the Court.

THE COURT: Sure.

MR. MASTRO: First, let me thank Your Honor for seeing us today. I had asked Mr. Miller to please afford us this opportunity, and I really appreciate the Court seeing us.

And as Mr. Miller pointed out --

THE COURT: It's not a problem. The adversary docket this afternoon is light, so it's perfectly fine.

MR. MASTRO: Thank you, Your Honor. It had, in fact, originally been our intention as we discussed at the last conference in April, when Your Honor said if we concluded that we think it was something appropriate to bring on to the Court, you're free to do it and we'll have it on the next regular date for hearing matters in adversary proceedings. We had tried to get this on for today. Mr. Miller and his team, for a variety of reasons, requested more time and we extended that professional courtesy to move it over to June the 16th. But I did want to ask Your Honor -- so in that regard we have agreed to a schedule. If it goes forward with the parties understanding for it to be on for the omnibus calendar for June the 16th. But I wanted to ask Your Honor if it might be possible, and I know how busy Your Honor has been, I know how demanding these cases are, I read everyday the important matters that Your Honor is dealing with and the ongoing hearing that Your Honor is having right now. If there were any possibility of us being seen earlier, I think Mr. Miller described that June 4th or June 7th would be possible dates, if the Court would entertain us.

But in any event, we're pleased to be back here on June 16th if that's the case.

I just also wanted to point out one other thing, Your Honor. That without getting into the merits now, there is a schedule in England with the Supreme Court which takes this out

to at least March of 2011. A decision sometime thereafter. So there are opportunities now for us to address some of the issues, since in England this has progressed to the highest appellate level. To address some of the issues here that we seek to raise with this Court, or potentially others.

So I really appreciate the Court's consideration. And as always, I'm grateful to be before the Court.

THE COURT: What's the argument in favor of expediting this?

MR. MASTRO: Your Honor, I think as Your Honor pointed out at the time you issued your original memorandum decision. Just to correct, Mr. Miller in one respect, we're a trustee with indemnification, so we are left vulnerable in that sense. And I did not understand the adversary proceeding to be that he was seeking money for his client, I understood it to be a declaratory judgment action, where Your Honor has already, through a memorandum decision, addressed the issues relating to declaratory judgment, without addressing remedy.

Your Honor, we see the expedition issue here being one where we do, as we made clear to Your Honor before and now in these motion papers, we have reviewed with our client our client's desire to be in a position to advance this case.

We see the larger ramifications. As Your Honor pointed out in his own opinion originally back in January that this is unprecedented in certain respects, that it covers new

ground, it is unique. And as the parties have acknowledged with Your Honor, the ramifications of this decision are significant not only for this case, but in other cases. This has far larger ramifications than this one case which is, itself, a very important case. So, Your Honor, we think that under all these circumstances, the ability to advance this case, especially with all the time that will now exist in England to advance review, we see it as -- Mr. Miller looks at it as well maybe what happens a year from now in England will moot the issue.

Correspondingly, Your Honor, there are appellate issues here that may change the dynamic in a way that relieves the conflict that exists between the English courts and this Court's decision. And we don't see it as at all inconsistent, Your Honor, with what you and the chancellor have said in exchanged letters, because there is nothing about Your Honor deciding this motion or, as we've requested, entering an order memorializing the memorandum decision, that would be at all inconsistent with what the chancellor has asked, which is simply that you take no action that would preclude entry of a judgment in England eventually.

So, Your Honor, for all those reasons, because of the larger ramifications, because we now are several months after your original decision and there is that opportunity for us to not only ask the Court to potentially reopen, but just as

importantly, in the first instance, for Your Honor to enter an order so that there would be a chance for review. There's no time like the present to do that, Your Honor. We would really appreciate the opportunity to do that. Thank you, Your Honor.

THE COURT: One more question.

MR. MASTRO: Certainly, Your Honor.

THE COURT: Are you making the request that this be expedited at the direction expressed or implied at perpetual?

MR. MASTRO: No, Your Honor. It is at the direction of my own client, a trustee without indemnification, who sees the profound ramifications for itself in this one instance, and also sees the profound ramifications in a lot of cases right now, where the decision that Your Honor issued that broke new ground, by all accounts, is now something that is having far-ranging ramifications. So my client feels very strongly about being able to take this at an appellate posture as soon as it can, now that so many months have passed.

THE COURT: Have you advised Perpetual that this is what you're doing?

MR. MASTRO: Your Honor, we have advised Perpetual of the motion that we filed, yes.

THE COURT: And has Perpetual encouraged you to prosecute this on an expedited basis?

MR. MASTRO: Your Honor, Perpetual has not given us a direction to do that. It has not given us a direction.

THE COURT: I'm not saying a direction, have they encouraged you? Do you have communication with them? Are you doing what you're doing on their behalf and with their, either tacit or express support?

MR. MASTRO: Your Honor, we're not doing it with their tacit or express support, we're doing it at our client's direction because our client perceives as a trustee of that indemnification that this is what our client should be doing.

THE COURT: I understand. But you're not directly answering my question either.

MR. MASTRO: I --

THE COURT: My question is to what extent -- I'll try it another way. Are you doing this with the knowledge that this is what Perpetual wants you to do?

MR. MASTRO: We are not doing it with the knowledge that this is what Perpetual wants us to do.

THE COURT: But are you doing it with the knowledge that Perpetual, while sitting on its hands, is, in fact, quietly encouraging this behavior?

MR. MASTRO: Your Honor, I want to be as clear as I can. They're not encouraging, they're not tacitly or expressly encouraging, and they've given us no direction. I don't know how to be any clearer than that, Your Honor. This is not --

THE COURT: Are you in regular communication with Perpetual regarding your strategy?

MR. MASTRO: Your Honor, as a trustee we advised them that we're doing this. And their response, Your Honor, they did not give us any directions or encouragement at all. Absolutely not. And I say that to Your Honor as an officer of the Court.

THE COURT: Okay, thank you.

MR. MASTRO: Thank you, Your Honor.

MR. MILLER: Your Honor, very quickly, I'd like to clarify a couple of points if I might.

First, Mr. Mastro suggested that LBSF is not seeking money. The Court is aware of the history and is aware of the fact that the English courts requested that the only issue to be placed before this Court at this stage, was an issue of declaratory judgment. But as we've said before on a number of occasions, LBSF envisions that if this matter does not become moot, it will ultimately need a remedy, and that remedy will certainly include a directive for disposition of funds. It's the position of LBSF that the money being held is property of the estate, and should be under the control of the estate.

However, there's certainly no way that BNY is going to get money paid to it as an entity. It's a question of where that money is going to go. It is a stakeholder. So in that sense, LBSF is the plaintiff.

We also believe, Your Honor, there is no conflict now with the English courts, because you have interpreted U.S.

Bankruptcy law and they are looking at English law. There may well be a conflict or there may never be a conflict. But Mr. Mastro's suggestion that appellate activity here might resolve a conflict, we don't believe there's any conflict that exists at this stage.

We would also point out, Your Honor, that we believe the best way to avoid the risk of conflict, is for this Court to retain control of the matter. Because this Court has the history of communications, and this Court understands the options that are available. And it is a bankruptcy court familiar with this entire estate and what its needs are.

We think that once it moves through the appellate process here that control is lost. There's really more potential for conflict to develop in an appellate court ruling of some kind, than in the present posture that this case finds itself in.

And, finally, Your Honor, this comment about he is a trustee without indemnification. I'm not an expert in the English proceeding. But my understanding is that the English Court has said there is an indemnification. But the scope of that indemnification is not yet to find. So we don't understand that BNY is without any assurance that there will be some kind of indemnification. Exactly what it will it will extend to and how it's going to be applied is something that that's still has to be defined. That is yet another way, Your

Honor, that this might become moot. It may be that BNY gets the indemnification, which we certainly believe they're entitled to. And if that's the case, then their concern will be alleviated.

So we do not believe that there is any need for expedition. And we believe that the Court's commitment to coordination, which it has already made and which has been requested by the English courts is the best way for this kind of a cross-border bankruptcy to be handled. Thank you, Your Honor.

THE COURT: Is there anything more?

MR. MASTRO: No, Your Honor. Thank you very much, Your Honor. I really appreciate it.

THE COURT: I see no reason to expedite this before the June 16th hearing. And for reasons that my calendar would actually propose that his be specially listed sometime after June 16 on a date to be determined in consultation with my chambers.

As Mr. Mastro alluded in his remarks, I'm involved in a fairly demanding litigation associated with the Barclays acquisition and we just completed the first two weeks of trial last week. That has been widely reported. What has not been widely reported is we are identifying a number of additional trial days in the month of June, and two of those days that have been identified but not yet formally scooped up by the

parties, but I expect these days will be, are the 14th and 15th of June. Which puts extra pressure on the Court in connection with preparing for all aspects of the June 16 omnibus hearing. This is not limited to Perpetual, this just relates to case management considerations. Additionally, and for reasons unrelated to mediations and proceedings in Delaware, I'm going to be overseas the week immediately before that hearing. Which will make it more difficult for me to prepare, I'm participating in an international insolvency conference in Italy. Everybody has to be somewhere. And for that reason the week before is problematic for me in terms of preparation.

So with that explanation having been put on the record, I would hope that the parties can identify some days that are available on my calendar in June after the 16th. Recognizing that I have already dedicated almost every available day to the Barclays' litigation. So my calendar is extraordinarily tight in June.

It's conceivable as a result that this could slip into July, but I will request that my courtroom deputy endeavor to accommodate this matter, perhaps on an afternoon when I already have a morning calendar.

Now, one of my concerns here involves the coordination with the courts in the United Kingdom. As indicated by Mr. Miller correspondence has been exchanged. I believe the parties have received copies of the correspondence. And the

most recent letter arrived about a week ago on very attractive blue stationery, which appears to be the trademark of the high court.

The request as characterized by Mr. Miller is that in effect I do nothing that may be open to interpretation. I do not consider it inconsistent with the request for cooperation from the high court that I hold a hearing in connection with the motion brought by BNY. Whether or not action in connection with the motion is deemed to be inconsistent with that request is something that I would like the parties to address at argument, in addition to the substance of the motion. And we'll deal with scheduling once you've had a chance to coordinate with my chambers.

Now, to the extent that the date for argument is later than the May 16th date, and it's possible to accommodate some of the scheduling concerns that Mr. Miller has identified that represent potentially a personal burden for him, I would hope that you would make appropriate accommodations to the briefing schedule, that also allows sufficient time for any reply papers that BNY might with to put in.

MR. MASTRO: Of course, Your Honor, we and we've tried to do that by saying we agreed to the 16th as a date for it as well.

And just so it's crystal clear, I'll be here whenever the Court can see us.

THE COURT: Fine.

MR. MASTRO: So hopefully it can be worked out more easily because I'll be here.

THE COURT: Fine. We'll endeavor to accommodate you on a special day, but I don't think it's going to be the 16th. It can be as close to the 16th as we can make it, but not that day. All right.

MR. MASTRO: Thank you, Your Honor.

MR. MILLER: Thank you, Your Honor. May the people who were involved with this first matter be excused?

THE COURT: Yes.

IN UNISON: Thank you for your time, Your Honor.

(Pause)

MR. SLACK: Good afternoon, Your Honor.

THE COURT: Good afternoon.

MR. SLACK: Richard Slack for the debtors.

The next matter on the calendar is the adversary proceeding brought by Neuberger Berman, which is case number 09-01258. And we're here for a status conference.

THE COURT: I've read the correspondence.

MR. SLACK: Okay. Your Honor, moving then if you've had the opportunity to do that, the status is essentially that the parties have had discussions about a scheduling order. We have proposed to the Court what I think is a fairly typical, yet aggressive, scheduling order that would provide for initial

disclosures to be filed within twelve days of today. Shortly after that it would provide, I would imagine, that the parties would serve written discovery, and then there would be approximately a three and a half month period for discovery.

PNC has opposed that. Has said, essentially, that they want a two-month period for discovery. And that's I think the nub of our communication. We proposed something slightly less than what we originally did. We thought five months was what we thought the appropriate amount was. At the beginning we were willing to come down and try to compromise. PNC has never sort of moved off their two-month period. We don't think that's an appropriate amount in this case.

And just two seconds on that, Your Honor. This case is really in some ways at its infancy. And that's because, as Your Honor is aware, just recently Your Honor approved the assignment between LBI and LBCC, which clarified the position of the debtors. At this point, Your Honor, we think it's appropriate for the case to move quickly. We think the schedule we've put in place does. There has not been initial disclosures.

The only discovery that's been provided so far, Your Honor, if Your Honor will recall at a previous hearing, we offered voluntarily to provide the transaction documents that show the back-to-back between Neuberger to Lehman, Lehman to PNC. That's been done. At that time we asked PNC to sign a

confidentiality agreement. We haven't heard back, that was in December of '09. We haven't heard back on that. But all of those matters are going to have to be done. We think the schedule gives plenty of time for the parties to do discovery and then move on to experts, and then summary judgment. And, frankly, the schedule has us completing all this up till trial by essentially the end of the year.

THE COURT: I have a couple of questions. One is has any discovery taken place in the interval while everybody's been arguing about how much time should be available for discovery?

MR. SLACK: The only thing that was done, Your Honor, was a number of months ago PNC served discovery requests. We said that we thought the parties should have a Rule 26 conference. We've said that we're prepared to do that and then move to discovery. For whatever reason, PNC has been unwilling to have that Rule 26 conference. And there hasn't been -- again, other than us producing the transaction documents, there hasn't been any other discovery.

THE COURT: All right. Two more questions. One is are you aware, and PNC can answer this question itself directly, but this goes to you Mr. Slack. Are you aware of any timing issues affecting PNC in the litigation pending in the Western District of Pennsylvania? That's question one.

Question two is I may be missing something as a result

of my review of the complaint, but this seems like a fairly simple matter. What discovery is really needed since either LBCC is or is not properly in the middle of this transaction?

MR. SLACK: The answer to the first question, Your Honor, is we're not aware of any scheduling matter. I know only what I've read in the prior pleadings from, frankly, last year, and nothing further, whether there's any other -- any other activity in that action, we don't know and we haven't been told by PNC.

With respect to the second, Your Honor, it is very possible that this is going to be a very simple matter. And I can tell you that from LBCC's standpoint, we believe it should be a very simple matter. We have provided the transaction documents. We think that the transaction documents show Lehman in the middle. I would point out, for example, that paragraph 13 of the interpleader complaint by Neuberger Berman says that Lehman is in the middle of this transaction. So we do believe that it's likely to be simple. And, frankly, we haven't seen the defense since the transaction documents were provided, we haven't seen any discovery. We don't know what PNC's defense of this is going to be. Are they going to claim that there are -- that there are other agreements, that those agreements don't say what they mean, that they're ambiguous. We have, at this point, no idea.

What I am worried about, Your Honor, is that it's

clear that we are going to have written discovery requests that go out. Those -- assuming we get the initial discovery out in two weeks, let's say, or twelve days, and then we can look at whatever comes in and get our written discovery out in the next ten days, two weeks, we're still talking about not getting the written discovery in in a normal situation, from about two months from now. And then you're going to have at least a handful of depositions. Assuming there's any issue at all with the Court, a three-month, three and a half month period, is a very expedited -- even without a lot of discovery occurring.

But I think the quick answer is, Your Honor, is the way we see this case is that this is a simple case, and that the words mean what they mean, and that the transaction documents mean what they mean. And that Neuberger's right in their complaint, and we're in the middle.

THE COURT: Okay. I'll hear what PNC has to say.

MS. GOLDMAN: Thank you, Your Honor. I'm Kathleen Goldman. I'm here today on behalf of PNC.

If I may I'd like to address some of the representations that Mr. Slack made with regard to the status of exchange of information in this case.

In September of 2009 we provided Weil and LBCC with all of the documents that PNC had relative to this trade. Neuberger Berman at that time also provided those documents. As far as PNC's concerned, we provided what we have. And so

when the parties were before the Court in November, and that was the first time that anyone mentioned any interest that Lehman may have in the trade between PNC and Neuberger Berman, we asked LBCC to actually provide those documents demonstrating this interest. At that time we also sent out the written discovery that Mr. Slack mentioned.

We did receive some documents which, quite frankly, we see no correlation between the documents provided and the trade at issue. But we did not get responses to our discovery. So we don't know if they have more documents or not. And LBCC's refused to respond to discovery saying that we need to have the pleadings closed, and we need to enter into a formal scheduling order. And that's all well and good, but the problem is this has been hanging out here now almost a year. It will be the anniversary, the filing of this action. I believe it was filed in the beginning of June of 2009.

And we were kind of stalled by LBCC's failure to recognize whether they, in fact, had a claim in this action. And the Court, in fact, retained jurisdiction simply because the representations of Mr. Slack at the previous hearing in November that they had a dog in this fight.

So as far as we're concerned all the documents have been exchanged, unless there's something else that LBCC has. And we believe that we would need three depositions, at most, which would be the corporate designees of the respective

parties, and that would be all that's really required.

What was missing from the letter that was sent to you last evening was the scheduling order that we provided in response to the scheduling order proposed by LBCC. In that scheduling order we asked for a discovery cutoff of factual discovery by July 15th. And then the exchange of expert witness information on July 15th and July 30th, respectively. And a close of expert witness discovery of August 30th. That way we'd be able to step this matter up for summary judgment, or an evidentiary hearing before this Court hopefully, and get this matter resolved, finally, by the end of the year.

I think in light of the fact that we've been stonewalled, essentially, since June of 2009, you know, we'd like to get this moving now. And the Court when we were before you last had asked us, you know, to cooperate with each other and see if we can start to sort out these very simple issues through cooperative action. And we've tried to do that and it's just not getting us anywhere, which is why we're here trying to get an order from the Court to get this thing finally off of center.

With regard to your question of Mr. Slack pertaining to where we are in the Western District action, the court there recently requested that we provide -- we being Neuberger Berman and PNC a status report. Unfortunately, the status report is that we're stuck in limbo here in the interpleader action. So

the court is anxious in the Western District for us to move this matter forward. And that's where we stand.

THE COURT: Okay. Do you wish to be heard on behalf of Neuberger Berman?

MR. RUBINSTEIN: Yes, Your Honor. Benjamin Rubinstein for Stroock & Stroock & Lavan, Neuberger Berman.

We just want to say that we also view this as a very simple matter. We'd like whatever discovery needs to be conducted to be concluded as quickly as possible. The longer we spend on this matter the more resources get burned through in our eyes. The most quickly this matter can be set for discovery is what Neuberger Berman would like. And in that sense we support PNC's proposal.

THE COURT: Okay. Mr. Slack.

MR. SLACK: I just have a couple of points.

My recollection, Your Honor, is that the only documents we received were the ones that were attached to the pleadings in the Western District. So we haven't received any other documents other than that.

With respect to the discovery I'm at a loss as to why we haven't heard back from PNC on the confidentiality order we sent in December. I have no idea why PNC has not agreed to have a 26(f) conference that we've been asking for for months. And I think the characterization of us as stonewalling is not only inaccurate it's wrong. And we want this case to be

moving, and it's just a question of given that we're at ground zero, essentially, how much time is -- how much minimum time do we need to still have a very quick discovery period. So we agree that this case should move fast. And I think our schedule does that, Your Honor.

THE COURT: I appreciate the positions that have been expressed here.

Let me state that, from my perspective, I'm both surprised and disappointed that the parties have been unable to work this out on their own. It seemed to me that just looking at the essential nature of this case that the issues are relatively simple, about as simple as anything that has been presented to me yet in the entire Lehman bankruptcy.

And the fact that this has not yet produced even an agreement on ordinary course pretrial order for is, frankly, a surprise.

I think that the schedule proposed by PNC is a little too aggressive. But probably in the right ballpark, that is the summer of 2010. Instead of July 15 I think August 15 would be a reasonable deadline for completing fact discovery.

You can make necessary adjustments to the schedule with that date in mind, perhaps bringing expert discovery into mid-September or a little bit later to take into account the Labor Day holiday. And you can be in a position then to either reach a settlement, present dispositive motions, or if there

are material issues of fact in dispute we can have a trial date. Now, when that trial date would be is another matter.

Recognize that just because you get through with discovery doesn't mean that you get here, assuming you haven't been able to otherwise resolve those.

So my direction is that the parties meet and confer with these dates as guidelines, and come up with what I think I have in each of my other adversaries in the Lehman cases, which is a relatively standard form of pretrial order. And Mr. Slack certainly knows the form for that. Is there anything more?

MR. SLACK: That's it, Your Honor. Thank you very much.

THE COURT: Okay. Then we're adjourned.

(Whereupon these proceedings were concluded at 2:41 p.m.)

I N D E X

R U L I N G S

DESCRIPTION	PAGE	LINE
Debtor's motion for authority to compromise controversy in connection with repurchase transaction with Fenway Capital, LLC and a commercial paper program with Fenway Funding, LLC granted	46	24
Motion of the SunCal debtors for relief from the automatic stay denied without prejudice as to the active litigation	74	20

C E R T I F I C A T I O N

I, Lisa Bar-Leib, certify that the foregoing transcript is a true and accurate record of the proceedings.

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LISA BAR-LEIB

AAERT Certified Electronic Transcriber (CET**D-486)

Veritext

200 Old Country Road

Suite 580

Mineola, NY 11501

Date: May 13, 2010